The Workings of the "Open" Multiple Employer 401(k) Plan

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A "Multiple Employer" 401(k) plan ("MEP"), where a single 401(k) plan is jointly sponsored by a number of unrelated employers, can often provide a cost effective way for some employers to manage their risks related to sponsoring a 401(k) plan, while enjoying advantageous pricing on investments and administrative services to which they may not otherwise have access.

These plans have generally been offered in the past through trade associations and, since 2002, Professional Employee Organizations (PEOs). There is now a growing number of service companies organizing MEPs without the use of trade associations or PEOs, as the marketplace seeks solutions to the costs and liabilities arising from the increasing complexity of retirement plan regulation. This non-traditional approach to MEPs is being met, at times, with skepticism as there is still some confusion related to the establishment, structure and proper operation of these "Open" MEPs -including the parties' respective roles, responsibilities, potential liabilities, and the design of provider compensation.

This confusion is understandable, because the rules governing MEPs are scattered throughout the Internal Revenue Code and ERISA, and are nowhere put together in any one spot in any sane or articulate manner.

This whitepaper addresses the issues giving rise to some of this confusion related to these Open MEPs. It is not intended to be a definitive technical manual, but a guide to help further the understanding of how these Open MEPs work. It will explain some of MEP's basic rules; identify matters that participating employers (referred to in this paper as the "PE", which is like the "Client Organization", or CO, of a participating employer in a PEO's 401(k)) and advisors need to know when joining a MEP; and to help lay out a framework under which an advisor or an employer can make thoughtful choices about the appropriateness of a MEP under any particular circumstance.

Key concepts

Background

MEPs have been commonly used for a very long time, and that there is confusion now can be, in itself, a bit confusing. The tax code rules governing these "Plans Maintained By More Than One Employer" (as MEPs are formally titled by the Code) are found in Tax Code Section 413, which was enacted by Congress as part of ERISA in 1974. The IRS first published regulations under this code section in 1977, but these regulations were actually made effective retroactive back to December 31, 1953. The regulations were last modified in 1979.

The use of MEPs dramatically increased in 2002, when the IRS settled a long running dispute with the PEO industry over the 401(k) plans sponsored by these organizations. A number of PEOs had taken the position that their 401(k) programs were "single employer" plans, as the PEO was the "co-employer" of their client organizations. The matter was finally settled with the issuance of Revenue Procedure 2002-21, where the IRS ruled that these plans would be treated as MEPs under tax code section 413(c), while laying out transition rules for PEOs to follow when transforming their "single employer" plans into MEPs.

What is a MEP?

Simply put, a Multiple Employer Plan is a 401(a) plan which is sponsored by more than one unrelated employer, which is covered under Code Section 413(c). It can be either a defined benefit or defined contribution plan, and is considered a single plan under both the Tax Code and ERISA. A single Form 5500 is filed for the plan.

[1]"Open" MEP is a term coined by TAG Resources, LLC, which describes a non-Association MEP. It includes both the TAG program as well as that of many PEOs, and does not require the membership in an employer organization as a condition of joining the MEP. TAG Resources, LLC commissioned this whitepaper.

Though the Code defines a MEP, ERISA itself does not actually define the term "multiple employer retirement plan." However, there are a number of references in ERISA and its regs to these retirement plans which have more than one sponsor, and which are not considered "multi-employer plans" related to collective bargaining agreements.

The MEP is NOT a "multi-employer plan." The Code and ERISA generally define collectively bargained retirement plans (including collectively bargained 401(k) plans) for multiple employers as "multi-employer plans", which are different than the "multiple employer plans" addressed in this paper. Those collectively bargained multi-employer plans are not subject to Code Section 413(c) but, instead, 413(a) and 413(b), and are treated much differently under ERISA than multiple employer plans. The laws surrounding those plans constitute a world to themselves, and are generally outside of the scope of this paper.

The special rules which apply to MEPs are actually quite simple and brief, even though they apply to a wide range of plans which include defined benefit and defined contribution plans. Though the rules themselves may be few and simple, much confusion has arisen related to how they actually apply to Open MEPs

A MEP is not a MEWA

It is important to not confuse a "Multiple Employer Pension Plan" (MEP) with a "Multiple Employer Welfare Arrangement", also known as a MEWA. A MEWA is a health plan (or other non-retirement "welfare plan" under ERISA) which covers the employees of several unrelated employers. MEWAs have a long and abusive history which has triggered significant legislation and regulation to address this marketplace abuse. Though there are some MEWA concepts that are useful in helping understand certain points under a MEP-such as the definition of an employer-much of the regulation related to MEWAs has very little to do with the MEP. Except in the discussion of the concept of "employer", it is best to generally ignore the MEWA rules when dealing with a MEP.

401(a), not 403(b) or 457

413(c) of the Code applies only to 401(a) plans; it does not apply to multiple employer 403(b) and 457 plans. Though these multiple employer 403(b) and 457 plans are possible, dealing with them involves addressing a number of issues related to the lack of 413(c); the manner in which ERISA applies (or doesn't apply) to many of these plans; and the legal complications under state and local law related to adopting government plans by multiple government entities.

These issues are not addressed in this paper, as the 401(a) MEP rules discussed here will apply in sometimes vastly different ways when applied to 403(b) or 457 plans.

Defined benefit plans

"Defined benefit" multiple employer plans have been commonly used in the past, and are subject to a number of unique rules relating to funding and pension insurance which do not apply to "defined contribution" multiple employer plans.

This paper focuses only on defined contribution multiple employer plans, and does not does not address issues related to the establishment and maintenance of defined benefit multiple employer plans.

Unrelated employers

A MEP under 413(c) can only be maintained by unrelated employers. Employers which are part of a controlled group of companies under Code Sections 414(b) or 414(c) are treated as a single employer for MEP purposes.

This means that companies under common ownership and control (as defined by 414(b) and (c)) can participate in a MEP only if there is another, unrelated company also adopting that MEP. A plan which is designed just for the companies within a controlled group of companies would NOT qualify as a MEP.

Collective Trust

Generally speaking, ERISA requires a collective trust or annuity arrangement where unrelated employers commonly invest their assets. However, a collective trust is not needed for a MEP, nor does participation in a collective trust cause a plan to be a participant in a MEP.

How a MEP is Structured

Anyone considering joining a MEP, or any one advising employers on joining, should be familiar with the basic elements of a MEP to make sure the MEP organizer is getting it right.

The rules for structuring MEPs are scattered throughout the law, but once found, they tend to be pretty simple, and straightforward, relying upon basic retirement law principles. But though the rules themselves may be simple, applying them properly requires a high level of skill-and there is still some ambiguity on some important points.

Authorization for MEPs.

The fundamental notion that a 401(k) plan can be sponsored by more than one employer is well established under both the Tax Code and ERISA. For example, the tax regulations[2] specifically authorizes multiple employer 401(a) plans to be treated as a single plan if all the "qualification" requirements for 401(a) are satisfied. The Code then lays out most of those tax rules for multiple employer plans in Code Section 413(c) and its regulations[3]; and ERISA Sections 3(16) (defining the term "Plan Administrator") and 210 (describing how hours of service are counted) ; and ERISA Section 104, related to benefit accrual, all make specific reference to these plans.

The MEP Setup

Certain specific requirements need to be met in setting up a MEP, of which the advisor or particpating employer should be aware.

- There must be an "Employer." Both ERISA[4] and the Code[5] require that the plan be established by an *employer or employee organization*. The IRS calls this employer the "Lead Employer"[6] (which we will sometimes refer to as the "LE" throughout this paper). Though the Tax Code does not actually define the term "employer" for these purposes, it is a defined term under ERISA. ERISA defines an employer as

  "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."[7]

  There are two ways for a MEP to meet this "LE" requirement. The first is that the MEP organizer can actually adopt the plan as an employer in its own right, for its own employees, and open it up for adoption by other employers. This would be the typical "Open" model, though it is possible for an Association to fall within this model if the plan covers the Association's own employees.

  The second way is for a group or association of employers- acting for an employer- to adopt a plan as the "LE." In order to be treated as an "employer," that group or association must meet the so-called commonality requirement.[8] This issue is discussed in further detail, below. This would be the common "Association" MEP model, where an industry trade group establishes a MEP for its membership under the control of its membership.

- The Lead Employer must have Employees. ERISA's regulations specifically state that the term "employee benefit plan" shall not include

  "any plan, fund or program, other than an apprenticeship or other training program, under which no employees are participants covered under the plan."[9]

  Similarly, the IRS has ruled that a MEP sponsor must have employees.[10] MEP organizers which cover their own employees, or which are "groups or associations" that are recognized as employers which cover their members' employees, both meet this requirement. A MEP organizer which sponsors a plan which has no employees likely fails this "employee" requirement

- Plan adoption. The LE adopts a plan document which must specifically, by its terms, support MEP status. MEP plan documents are not eligible under the IRS's master and prototype program, but can be submitted using the volume submitter program. The IRS procedures entitle adopting employers to rely upon the determination letter issued to the LE, though permits the LE to request (for a fee) a separate determination letter be issued to each PE separately.

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[2]Treasury Reg 1.401-1(d)
[3]Treas. Reg 1.413-2
[4]ERISA 3(2)(A)
[5]Treas. Reg 1.401-1(a)(3)(ii)
[6]EP Determinations Quality Assurance Bulletin, FY2004 No. 2, June 4, 2004
[7]ERISA Section 3(5)
[8]See, for example, DOL Advisory Opinion 89-17A, where it is reviewed in the context of a MEWA.
[9]29 CFR 2510.3-3(a)
[10]Rev. Proc. 2002-21, Section 3.03 states "Exclusive benefit rule. Section 401(a)(2) provides that a trust forming a part of a qualified pension, profit-sharing, or stock bonus plan must be a trust established and maintained by an employer for the exclusive benefit of that employer's employees and their beneficiaries ("exclusive benefit rule"). Therefore, a retirement plan that provides benefits for individuals who are not employees of the employer maintaining the plan (and who are not otherwise treated as employees under rules such as those under § 414) violates the exclusive benefit rule and does not satisfy the requirements of § 401(a)."

- Failure of "employer and "employee" rules. Should the MEP fail to meet the "employer" and "employee" requirements, it will not be recognized as a MEP, and all the participating employers will likely be seen as maintaining their own plans. This could cause a "plan document" failure needing to be corrected under the IRS's correction program; potential violation of ERISA's anti-inurement rule under ERISA 403(c) (which not only prohibits employer benefit, but also requires that the assets of a plan only be used for the purposes of that plan[11]); possible prohibited transaction concerns; and Form 5500 issues.

Joining the MEP

The employer which decides to join a MEP is legally adopting the plan as its own, becoming a co-sponsor of the MEP along with the other PEs and the LE. The PE will sign a joinder agreement which serves like an adoption agreement of a prototype plan, under which it will identify the terms of the plans which will apply to its employees. The joinder agreement may also outline the delegation of authority necessary under the plan to make the particular MEP program work.

- Existing plans. Existing plans adopting the MEP will be merging their current plan into the MEP, adopting that new document as its own. This is more than a simple restatement; it is an actual merger of plans. The PE will file a final Form 5500 on its old plan and, in most cases, the Form 5310-A will not be required to be filed.

- New plans. An employer not currently sponsoring a plan, which then joins the MEP, is merely adopting the MEP as its own new plan. It will sign the joinder agreement in the same manner as it would if they were adopting a prototype plan, relying upon the same corporate authority as would be required to adopt any new 401(k) plan.

- Delegating authority. Proper delegation of authority under the MEP is key to making the program work successfully.

  The PE is a plan sponsor, but care should be taken that any statutory obligations of a Plan Sponsor be assigned to the LE. It is also critical for the LE to have the status of Plan Administrator and Named Fiduciary-with the right to delegate other fiduciary obligations.

  This means that the plan document itself should name the LE (whether it be the Association plan's governing body or the Lead Employer on a Open MEP) as the Plan Sponsor, Plan Administrator and Named Fiduciary. Failure for this delegation to occur in the plan document could, in some instances (such as in certain Association plans) cause the PEs to be considered Plan Administrators. The LE should reserve to itself the right to amend and/or terminate the plan, while protecting participant rights.

  PE's, however, are not totally without rights and obligations under the plan document. PEs need to have the right to terminate their participation in the plan by directing the LE to spin off its assets; and employers will want to reserve to themselves a reasonable right to notice of amendment and termination as well. In certain circumstances, the PE will be a fiduciary (albeit with limited responsibilities) with regard to the portion of the MEP which covers its employees.

  The relative rights and obligations of the LE and the PE should be well documented to minimize any confusion, and can be done in either the document by which the PE adopts the plan, or by a separate agreement between the LE and the PE where specific delegations, representations, disclosures and approvals are undertaken.

- Terminating MEP participation. A PE which decides to leave the MEP accomplishes this by directing the LE to spin off the portion of the plan which is related to its employees into a new plan. The PE will need to establish the new plan, and the subsequent transfer of assets is considered a spin-off and plan-to–plan transfer. It is not considered a termination of the PE's plan, and therefore not a distributable event for elective deferrals.

  Where a PE wishes to completely discontinue its offering of a 401(k) plan to its employees, the LE will generally spin off that PE's assets into a new plan which is then immediately terminated. This results in a clearly allowed distributable event. The MEP plan document should reserve to the PE this right to spin-off.

  Though some commentators have noted that it may be possible for a MEP to reserve the right "partially terminate" the PE's portion of the plan at the PE's instruction, and then fully vest and distribute those funds, there is nothing in the Code or regs which identify the partial termination of a MEP (or any plan) as being a distributable event for elective deferral distribution purposes. Absent further guidance, the better defined alternative is to spin-off an then terminate.

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[11]See, for example, a U.S. Court of Appeals case, Jacobson v. Hughes Aircraft, 103 F3d 1288 (9th Cir. 1997).

Where the PE is not being cooperative, and the LE needs to disgorge the PE from the plan, the LE may also use plan language which grants it the right to establish a new "spin-off" plan for the PE, terminate it and make distributions

Specific MEP plan rules

Certain technical rules apply to the MEP on a consolidated basis, and certain rules apply on a PE by PE basis. Without providing an exhaustive list, the following apply:

- Code Sections 410(a) & 411. All service for any PE in the MEP must be counted toward that employee's current PE for purposes of eligibility and vesting.
- The following is applied on a PE by PE basis, as if each were maintaining a separate plan: highly compensated employee status; top heavy status; discrimination testing (ADP and ACP); coverage testing under 410(b); ERISA's benefit accrual requirements and 404(a) deduction limitations.
- A single Form 5500 is filed, and a single audit at the MEP level is required.
- A plan document is required to be made available at each PE.
- Though the LE would generally be the Responsible Plan Fiduciay with regard to the new 408(b)(2) service provider fee regulations, each PE would also have that role with regard to the appointment of the LE as Plan Administrator.

Benefit structures

A MEP may allow each PE to maintain its own benefit formula as long as it meets the coverage and discrimination rules, tested as if it were a single employer plan. This includes things like matching formulas, and whether they are discretionary or not; employer discretionary contributions; and adoption of automatic enrollment. Each can have its own vesting schedules as well, as long as all of the hours of any employee with any PE are counted toward the vesting requirements under the current PE's arrangement.

A MEP may limit the availability of any of the choices as a matter of plan design.

Commonality and the MEP

The issue of "commonality" regularly arises with regard to the discussion of a MEP. It is often mistakenly used to describe the incorrect notion that employers are required to have a "common employment bond" before participating in an Open MEP.

The MEP structure, unlike the MEWA structure upon which much of the "commonality" rulings in the past are based, only require "commonality" if an association seeks to sponsor a MEP. Though the DOL has yet to publish guidance on this issue as applied to MEPs, if employers, with employees, are co-sponsoring an Open MEP, no commonality between those employers appears to be required by law.

Code Section 413(c) is unique in that, unlike a MEWA, it recognizes the establishment of a single plan by multiple, unrelated employers. It does not require that each of these employers be part of an association, or that they have any common employment bond. In fact, it requires that the employers be unrelated. What both the Code and ERISA do require, however, is that each participating employer in the MEP actually have employees- or former employees-which are covered by the plan. Legally, then, each employer is viewed as a co-sponsor of the single plan where they are each required to recognize its own employees' service with any other PE (arguably, a stronger "employment related bond" than that required of an association MEWA). They do not need to resort to the use of an association.

Commonality only becomes an issue when a group or association of employers, acting as a single organization, seek to sponsor a plan for the collective benefit of their member's employees (this was necessary for MEWAs because of the lack of a law recognizing the joint action of employers as under 413(c), but is not necessary to make a MEP work). That joint organization may not have employees themselves covered by that plan. For these sorts of organizations, the commonality issue is critical to make the MEP work. The DOL describes it well in their DOL Advisory Opinions on MEWAs:

"The definitional provisions of ERISA thus recognize that a single employee welfare benefit plan might be established or maintained by a ***cognizable, bona fide group or association of employers***, within the meaning of section 3(5), ***acting in the interests of its employer members to provide benefits for their employees***. On the other hand, where several unrelated employers merely execute similar documents or otherwise participate in an arrangement as a means to fund benefits, in the absence of any genuine organizational relationship between the employers, ***no employer association***, and consequently no employee welfare benefit plan, ***can be recognized***."[12] (emphasis added).

Where, on the other hand, an employer adopts a MEP under 413(c) for its own employees, and delegates the Plan Administrator and Named Fiduciary roles to the Lead Employer while retaining oversight obligations, it is not attempting to establish a "genuine organizational relationship" which is covered by these DOL rulings. It is acting on its own behalf, in a plan where it is required to recognize the employer is required.

With the DOL not yet ruling on this issue as it relates to MEPs, there is still some ambiguity in the application of these rules. So it is also important to keep in mind that the policy considerations underlying the regulation of a MEP are starkly different from the policy considerations underlying the regulation of a MEWA. Many MEWAs were abusive, and were designed to use ERISA as a way to circumvent the application of valuable protections under state insurance law which, in turn, led to the development of a commonality standard designed to stop abuses. The properly designed Open MEP does not engage in such abuses and, instead, embraces responsibility.

Is the Participating Employer a Fiduciary?

Fiduciary Status

The most controversial issue for which there seems to be no clear answer which can be uniformly applied is whether or not the PE has any fiduciary obligations with regard to the MEP. A number of commentators have taken the position that the adoption of the MEP is merely a "settlor" function, which means that it is a decision of the employer which is not subject to ERISA's fiduciary standards. For MEPs sponsored by Associations, where the Association itself is deemed to be the acting in the role of employer, this may be particularly true under a hyper-technical reading of the law.

MEP organizers taking this position should do so carefully, however. Even should they prevail in their assertion that PEs are not fiduciaries, and thereby avoiding fiduciary liability, there is a serous downside to this position. If the choice of the MEP and its attendant investment platform is not an ERISA fiduciary act, the PE also loses the protections available to them under ERISA. Decisions to adopt a plan into which its employees' funds are deposited (particularly if there is automatic enrollment) will expose the employer to potential state law claims of negligence, employment law and contract law violations , together with claims for punitive damages. None of these actions are available to participants should they bring suit against an ERISA fiduciary, as ERISA pre-empts these state law claims.

For the Open and PEO MEPs, the "non-fiduciary" position is difficult to justify. Though the decision to adopt a plan is clearly a settlor function, MEPs come as a package which involves making a choice of a Plan Administrator, a Named Fiduciary as well as the plan investment platform. These, on their face, appear to be fiduciary acts of an employer.

Just as important, however, is the impact on compensation arrangements. For the MEP organizer (who is also the Lead Sponsor of the MEP) to receive compensation, the PE must bear a fiduciary role in approving that LE compensation. This issue is discussed in detail later in this paper.

Limited Fiduciary Role

One of the attractive features of the properly designed MEP is that it can serve to substantially minimize- though likely not eliminate- the PE's fiduciary exposure. The PE will appoint the Plan Administrator and the Named Fiduciary, to whom will be delegated the obligation to hire and monitor the investment advisor, the investment manager and the TPA. With the right design, the PE's fiduciary responsibilities can be limited to these: to select the MEP, appoint its fiduciaries, and approve of its investments MEP fees; and to periodically monitor the delegations mentioned above.[13] The PE also has the ongoing obligation to timely remit contributions to the plan.

PEs adopt MEPs, in part, to minimize their involvement in their 401(k) plans to the extent legally and prudently possible. Their ongoing monitoring function is not the same, for example, as would be expected of the Investment Committee of a single employer plan which would be responsible for continually monitoring plan investments. The focus of the PE's ongoing responsibility is to periodically look for information from the LE to demonstrate they are prudently performing their delegated functions (such as the LE regularly monitoring of investment performance). This task is something which the LE should be able to readily accommodate.

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[12]DOL Advisory Opinion 89-17A, August 17, 1989.

[13]The DOL has useful information on this topic at http://www.dol.gov/ebsa/publications/fiduciaryresponsibility.html where it instructs that delegating responsibility involves the ongoing responsibility to monitor the fiduciary to make sure it is acting prudently with its appointment.

Other Major Issues

Compensation

Properly compensating the parties involved in operating the MEP is a critical issue, as failure to do so could result in a violation of ERISA's and the Tax Code's prohibited transaction rules. The most noteworthy aspect of these rules is that they are inherently factually based. A small change in the facts can be the difference in a prohibited transaction occurring or not.

The prohibited transaction rules are the conflict of interest rules which apply to most non-governmental and non-church retirement plans. They effectively will not allow a fiduciary to engage in a financial transaction with a "party in interest" to the plan without it being permitted by statute, regulation or administrative ruling; nor can the fiduciary engage in a transaction for its own self interest unless an exemption has been granted.

To determine whether any Open MEP's compensation practice falls within these rules, the parties' respective roles in the MEP must be identified (note that the analysis may be different for a MEP sponsored by an Association).

Where the LE has been appointed as the Plan Administrator and Named Fiduciary to the portions of the MEP applicable to the appointing PE's employees, it is a fiduciary (and thus a "party-in-interest" to the plan) to those portions of the MEP. The PE is a fiduciary with regard to the appointment of the LE as Plan Administrator and Named Fiduciary to the portion of the plan covering PE's employees.[14] The LE is the Plan Administrator and named Fiduciary, without being appointed by a PE, to the portion of the plan covering the LE's own employees. Given these relationships, here's how the compensation rules apply:

- Sales/Marketing compensation. If the LE is the MEP organizer, as is typical in an Open MEP, it generally cannot take on the role of "fiduciary" in the sale of the MEP program to a PE and receive compensation for it. This is because there would be an inherent conflict in advising that the PE choose the program which generates income to the LE, if that LE (or its affiliate) is acting as a fiduciary under the MEP. The LE also cannot receive sales compensation on the portion of the plan related to its employees; it is unlikely to meet any applicable prohibited transaction exemption.

- Compensation as Plan Administrator. A MEP organizer which also is the LE is the employer for ERISA prohibited transaction purposes with regard to the assets of the plan covering its own employees. This means that it will not be able to receive compensation directly or indirectly from the plan related to its employees' assets unless it meets the prohibited transaction exemptions related to reimbursement of direct costs.

  This LE is not, however, the employer with regard to the PE's employees.[15] This enables it to receive direct and indirect compensation from the plan as a fiduciary as long as it's authority is delegated to it, and compensation approved, by the PE (acting as a fiduciary), and as long as it otherwise meets the requirements of ERISA Section 408(b)(2).[16] 408(b)(2) requires that the LE compensation be disclosed to and approved by the PE, which should be done as part of the joinder process.

- Investments. The LE or an affiliate may be able to serve as investment advisor or manager with regard to the MEP, and receive compensation for those services, under limited circumstances. The appointment to those roles need to generally follow the rules outlined above for Plan Administrator, but would result in increased monitoring obligations of the PE. If the compensation for these services is paid from revenue from the investment provider rather than from the plan itself, the compensation needs to be level (a difficult task when offering a NAV platform) and the plan needs to be structured in such a way that the PE's choice to adopt, and to stay in, the MEP is also a PE fiduciary choice with regard to the investment platform offered under the MEP.

Disqualification

One of the risks related to a PE adopting a MEP is that any other PE which violates any of the disqualification rules can potentially disqualify the entire MEP. This risk is manageable because of the IRS's corrections program, the Employer Plan Compliance Resolution System, or EPCRS.

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[14]Note that a fiduciary generally only has responsibilities with regard to the portion of the plan over which it exercises control. Thus, the PE is only a fiduciary with regard to the appointment of the Plan Administrator and named Fiduciary over the assets covering its own employees. This limiting language should also be in the plan document.

[15]There are references in Code Section 413(c) to treating "all employees of each employer who maintain the plan were employed by the same employer," but this language specifically only applies to the application of certain Code sections-not including those governing prohibited transactions.

[16]The new regulations for service provider fee disclosure under 408(b)(2) are effective, generally, January 1, 2012.

EPCRS permits employers to self-correct insignificant qualification errors without filing with the IRS; establishes a "Voluntary Correction Program" by which plans can voluntarily correct significant disqualification problems with relative ease; and the "Audit Closing Agreement Program," where a plan that would otherwise be disqualified on audit can negotiate a reasonable settlement with the IRS.

The IRS' corrections programs permit a plan to cost-effectively correct the PE's "disqualifying" error without jeopardizing the plan's qualified status. In that the correction would involve just the portion of the MEP which was affected by the "disqualifying PE," other PEs would not be impacted by such corrections.

The plan documents or other agreements should hold that "disqualifying PE" responsible for the costs of correction, and should permit the Leading Employer to spin-off any such portion of the plan. In the absence of the PE being able to pay the cost of corrections, the LE will likely be responsible for that cost. In any event, the actual disqualification risk to the PE under a professionally managed MEP may, as a practical matter, be less than the risk in the PE maintaining its own single employer plan.

"All assets" issue

The tax code defines a "plan" as one which meets the requirements of Section 414(l), and that all of the assets of the plan be available to pay all of the benefits of the plan. Literally read this appears to make all of the PEs in the plan a sort of "guarantor" of all the other PEs.

In a defined benefit MEP, this would clearly be the circumstance. However, in a defined contribution plan structure with individual accounts, it would be a fiduciary breach to invade participant accounts in order to make other participant accounts whole. This MEP problem of "all assets" is a problem which is common to any individual account defined contribution plan, including single employer plans.

Though the IRS has not directly addressed the issue, it has implicitly recognized the individual account MEP as a single plan in Rev Proc 2002-21. Though it is not definitive, it appears that an MEP, acting in a manner consistent with a single employer plan-such as maintaining a uniform investment platform; where all of the plan assets are available to operate the plan where necessary; centralized fiduciary control; and where all of the assets of the plan are available to pay all of the expenses-may be sufficient to address this long standing concern.

As Open MEPs become more widely used by employers seeking cost-effective ways to provide their employees retirement plans, we should expect to see increased regulatory activity which should, over time, help clarify a number of the open issues.

Any discussion on any tax issue addressed in this whitepaper is not intended to be used, and cannot be used, for purposes of avoiding penalties imposed under the United States Internal Revenue Code or promoting, marketing or recommending to another person any transaction or tax-related position addressed therein. Further, nothing contained herein is intended to provide legal advice to any party, and readers should consult with their own legal or tax counsel when dealing with these issues.

Bob Toth has 25+ years of experience in employee benefits law. His practice focuses on the design, administration and distribution of financial products and services for retirement plans, one which combines elements of ERISA, tax law, insurance law, securities law and investment law for both 401(a) and 403(b) plans.

Bob's experience includes implementing 403(b) programs under the new regulations; designing investment products for 401(k) plans; annuitization programs for defined contribution plans; advising on prohibited transactions issues related to retirement plan products and services and their distribution, development of open architecture programs for 403(b) plans and writing and implementing standards for fiduciary and advisory practices.

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