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SECURE ACT: POOLED EMPLOYER PLANS AN INTRODUCTION

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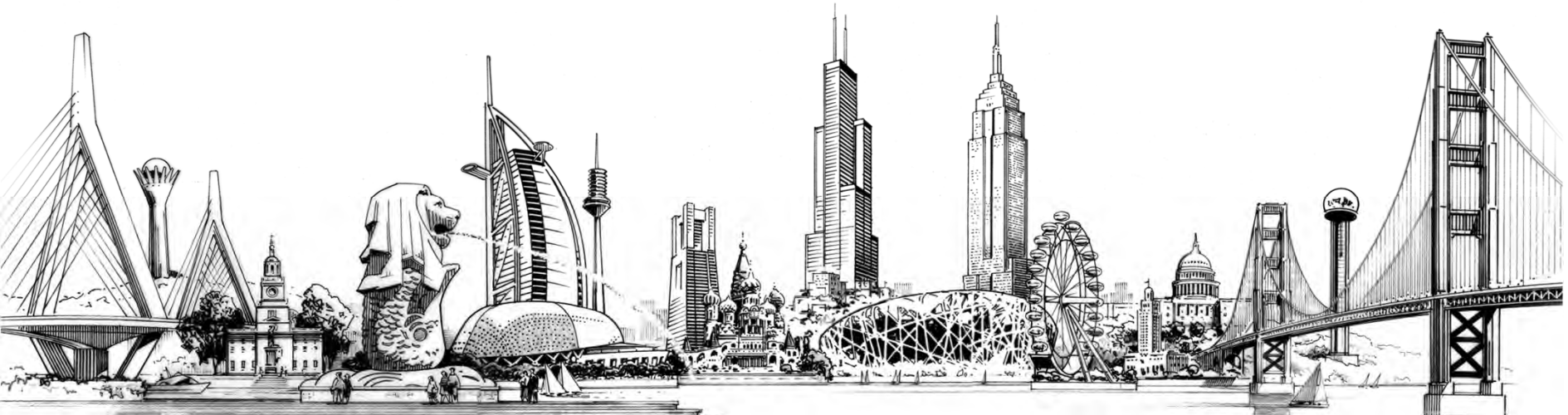

The SECURE Act

- The SECURE Act and RESA, which included many similar provisions, had been under consideration in the House and Senate since early 2016.
- The current iteration of the SECURE Act passed the House in July 2019 (by a vote of 417-3), but had been held up in the Senate, until –
- In December 2019, the Senate included the SECURE Act in the Further Consolidated Appropriations Act, 2020, which President Trump signed into law on December 20, 2019.
- This brings about a number of long-heralded changes, including the creation of the pooled employer plan (PEP).
  - Generally, PEPs are centrally administered defined contribution plans that can be joined by multiple unrelated employers.

Before PEPs, MEPs

- Before discussing PEPs, it is important to discuss traditional multiple employer plans (MEPs).
- MEPs are centrally administered retirement plans in which multiple "employers" participate.
- The Department of Labor (DOL) has read into ERISA's definition of "employer" a requirement that adopting employers of a MEP share an "employment based common nexus" and exercise control over the MEP.
- The commonality requirement was recently simplified through 2019 DOL final regulations (describing so-called Association Retirement Plans) that superseded prior subregulatory guidance.
- Traditional MEPs are not to be confused with plans covering different companies that are part of a "controlled group," or with multiemployer plans.

The History of "Open MEPs"

- It is now widely accepted that MEPs require adopting employers to satisfy the commonality and control requirements, but this was not always the case.
- Prior to Advisory Opinion 2012-04A, many MEP sponsors took the position that unrelated employers could participate in a MEP.
- Advisory Opinion 2012-04A determined that an allegedly open MEP was actually a collection of separate plans that utilized the same plan document and plan administrator; it introduced the commonality and control requirements.

Calls to Re-Open MEPs

- Since the moment Advisory Opinion 2012-04A closed the door on open MEPs, people have been calling for the return of open MEPs.
- Advocates for open MEPs argue that MEPs provide a great vehicle to help small business owners and their employees save for retirement, and that MEPs provide significant economies of scale and scope.
  - Both the Obama Administration and the Trump Administration sought to expand access to MEPs.
- Recent IRS and DOL regulations helped increase access to MEPs, but they stopped short of open MEPs.
- The SECURE Act's PEPs get much closer – providing something like pre-2012 open MEPs, but within a specific framework and subject to additional oversight.

Amendments to the Internal Revenue Code

- The SECURE Act revises the Internal Revenue Code of 1986 (the Code) to introduce a new section 413(e).
- It also made minor conforming and technical amendments to Code sections 413(c)(2) and 408(c), respectively.
- The new Code section 413(e) is described in detail below.

Amendments to ERISA

- The SECURE Act amends the Employee Retirement Income Security Act of 1974 (ERISA), sections 3(2), 103(g), and 412(a), and adds new sections 3(43) and 3(44).
  - Section 3(2), the definition of "employee pension benefit plan," was the source of the "commonality" requirement that the DOL had read to prevent the creation of "open MEPs."
- It also makes minor amendments to ERISA sections 3(16)(B), 3(41) and 103.

Who Cares About PEPs?

- Potential Pooled Plan Providers (PPPs)
  - PEPs create a new, potentially significant market for aspiring PPPs.
- Small and mid-sized employers (including tax-exempts)
  - PEPs allow for significant economies of scale and scope.
  - PEPs remove significant administrative burdens.
  - PEPs can help avoid state-mandated savings schemes (through preemption).
- Service providers that may service PEPs or adopting employers
- Employers looking to outsource retirement plan responsibilities
  - PEPs impose relatively limited administrative responsibilities on adopting employers.
  - PEP rules may also limit (but do not eliminate) fiduciary responsibilities of such employers.

Who Could Not Care Less?

- Employers who desire significant control over the design and administration of their plan
- Employers that do not expect to benefit significantly from the economies of scale or scope that PEPs could provide
- Employers that want all the bells and whistles in their plans
- Employers that are not interested in sponsoring an individual account plan for the benefit of their employees
- Bargaining parties seeking to establish a multiemployer plan (which may not be a PEP)

What is a PEP, Generally?

- Generally, PEPs are centrally administered defined contribution plans that can be joined by multiple unrelated employers.
- The PEP will be established, maintained, and administered by a pooled plan provider (PPP).
  - The PPP will likely be a retirement services firm (such as an insurance company, bank, trust company, consulting firm, recordkeeper, or TPA).
- The SECURE Act imposes specific requirements on PEPs and PPPs.
  - As indicated, these provisions appear in both the Code and ERISA.

What is a PEP, Specifically?

- The Code does not define a PEP, instead referring to MEPs that have PPPs.
- ERISA defines a PEP to be a Plan:
  1. That is an individual account plan established or maintained for the purpose of providing benefits to the employees of 2 or more employers,
  2. That is tax qualified under Code section 401(a) or a Plan that consists of accounts described in Code section 408, and
  3. Whose plan document includes certain specified terms.
- These definitions do not permit defined benefit PEPs, and do not appear to envision 403(b) PEPs.

What is a PEP, Specifically? (continued)

- Multiemployer plans (which are distinct from MEPs, and which require the plan to be maintained pursuant to one or more collective bargaining agreements) cannot be PEPs.
- Plans established prior to December 20, 2019 cannot be PEPs, unless the plan administrator of such plan elects for the plan be treated as a PEP and the plan meets the requirements of a PEP.

What is a PPP, Generally?

- It is the entity responsible for establishing and administering the PEP.
- The PPP serves as a named fiduciary and the administrator of the PEP.
- We anticipate that retirement services firms of different types (insurance companies, banks, trust companies, consulting firms, recordkeepers, TPAs) will consider becoming PPPs of PEPs.

What is a PPP, Specifically?

- The Code and ERISA define a PPP as a person (or entity) who:
  1. Is designated by the plan document as a named fiduciary, the plan administrator, and the person responsible for performing all administrative duties that are reasonably required to ensure that the PEP, and each adopting employer, satisfies the applicable requirements of ERISA and the Code;
  2. Registers as a PPP with the IRS and DOL, and provides any information the IRS and/or DOL require before beginning operations as a PPP;
  3. Acknowledges in writing that he or she is a named fiduciary and the plan administrator of the PEP;
  4. Is responsible for ensuring that all persons handling PEP assets are properly bonded in accordance with ERISA section 412.

What is a PPP, Specifically? (continued)

- PPPs are subject to audits and investigations by the IRS and DOL.
- For purposes of determining who is a PPP and whether the requirements described in the prior slide are satisfied, all persons treated as a single employer under the controlled group rules are treated as the PPP.
- The PPP is treated as the PEP sponsor for the administrative duties imposed on it.
- Each adopting employer is treated as the PEP plan sponsor (with respect to such employer's participants and beneficiaries) for all other purposes.

Required Terms for a PEP

- ERISA requires the PEP plan document to:
  - Designate a PPP and provide that the PPP is a named fiduciary of the PEP.
  - Designate one or more trustees to be responsible for collecting contributions to, and holding the assets of, the PEP.
  - Require the trustee(s) to implement written contribution collection procedures that are reasonable, diligent, and systematic.
  - Provide that adopting employers, participants, and beneficiaries are not subject to unreasonable restrictions, fees, or penalties with regard to ceasing participation, receipt of distributions, or otherwise transferring assets of the PEP as permitted under ERISA.

Required Terms for a PEP (continued)

- ERISA further requires the PEP plan document to provide that each adopting employer retains fiduciary responsibility for:
  1. The selection and monitoring of the PPP and any other person who, in addition to the PPP, is designated as a named fiduciary of the PEP.
  2. The investment and management of the portion of the PEP's assets attributable to the employees of the adopting employer, to the extent not otherwise delegated to another fiduciary by the PPP and subject to ERISA 404(c) (regarding participant directed accounts).
- This means that the fiduciary responsibilities of adopting employers may be limited to the prudent selection and monitoring of the PPP.
  - Whether these responsibilities will be limited depends on the precise terms of forthcoming DOL guidance.

Required Terms for a PEP (continued)

- ERISA further requires the PEP plan document to provide that:
  - The PPP is required to provide to adopting employers any disclosures or other information the DOL requires, including any disclosure or other information to facilitate the selection and monitoring of the PPP by the adopting employers.
  - Each adopting employer is required to take such actions as the DOL or the PPP deem necessary to administer the PEP or for the PEP to meet any applicable requirement under ERISA, Code section 401(a), or Code section 408, as applicable, including providing any disclosure that the DOL requires or the PPP determines is necessary to administer the PEP or allow it to satisfy these applicable requirements.
  - Such disclosures may be provided in electronic form and will be designed to ensure only reasonable costs are imposed on PPPs and adopting employers.

Model Plan Language

- The Code does not impose specific plan document requirements on PEPs.
- However, the SECURE Act directs the IRS to publish model plan language that meets the requirements of Code section 413(e) and the applicable provisions of ERISA.
- It is not clear when this model language will be issued, or how extensive it will be, but good faith compliance will be sufficient until it is issued.

PEPs Excluded from One Bad Apple Rule

- Code section 413(c) provides that, in the case of a plan maintained by more than one employer, certain qualification requirements (and other rules) apply as though each employer was the employer that sponsored the plan.
- This has been interpreted to create the "one bad apple" rule.
  - This results in the disqualification of the entire plan if a single adopting employer fails to satisfy a qualification requirement.
- New Code section 413(e)(1) provides that notwithstanding this rule, PEPs and certain traditional multiple employer plans (MEPs) will not be disqualified merely because one or more adopting employers fail to satisfy the qualification requirements.

Conditions for the Exclusion

- Generally, this exclusion from the one bad apple rule is only available if:
  1. The PPP transfers assets attributable to the employees of the employer that is causing the qualification failure to an IRA (or to any other arrangement the IRS determines is appropriate).
  2. The employer that is causing the qualification failure remains liable for any liabilities to the PEP attributable to the employees of such employer.
- If the PPP fails to perform its administrative duties, the IRS may choose to disregard the exception to the one bad apple rule (even if the conditions described above are met) and disqualify the PEP.

PEPs Excluded from Commonality Requirement

- ERISA's definition of pension plan was amended to address PEPs.
- Specifically, a new subsection has been added that treats PEPs as:
  1. A single employee pension benefit plan, and
  2. A plan to which ERISA section 210(a) applies.
- ERISA Section 210(a) describes how ERISA applies to MEPs.
- In effect, this amendment excludes PEPs from ERISA's commonality requirement.

Fidelity Bonding Requirement

- ERISA requires every fiduciary of an employee benefit plan and every person who handles plan assets to be bonded.
- The SECURE Act amends ERISA section 412(a) to provide that the maximum amount of a bond required for the fiduciary of a PEP is $1,000,000 (instead of $500,000, which is the maximum limit for plans that do not hold employer securities).

Form 5500 Reporting

- In addition to the other information required to be included in a Form 5500, PEPs (and MEPs) must include:
  1. A list of adopting employers and a good faith estimate of the percentage of total contributions made by each such employer during the plan year and the aggregate PEP account balance attributable to each employer
  2. The identifying information of the PPP
- Generally, a pension plan may only file a Form 5500-SF if it covers fewer than 100 participants. But, if a PEP (or MEP) has fewer than 1,000 participants and no single adopting employer has 100 or more participants in the PEP (or MEP), then the PEP (or MEP) may file a Form 5500-SF.
  - Technically this requirement allows the DOL by regulation to permit PEPs to file Form 5500-SFs. Until such a regulation or other guidance is issued, presumptively all PEPs should file Forms 5500.

Recap of Key Code Provisions

- PEPs are defined contribution plans with more than one adopting employer and a PPP that administers the PEP.
- Anyone can be a PPP, if they satisfy certain conditions.
  - Plan document requirements
  - Register with IRS before acting as PPP
  - Acknowledge named fiduciary and plan administrator status
  - Ensures proper bonding of all individuals handling plan assets
- One bad apple rule is eliminated for PEPs, as long as the assets attributable to the offending employer are spun off and merged out.
- Model plan language is forthcoming.

Recap of Key ERISA Provisions

- PEPs are exempt from the commonality requirement that applies to MEPs.
- ERISA has extensive requirements for PEP plan documents.
- Fiduciary responsibility for adopting employers may be limited to the duty to select and monitor the PPP, depending on forthcoming DOL guidance.
- ERISA's PPP requirements are similar to the Code's requirements.
- ERISA bonding is required for all PEP fiduciaries (up to $1MM).
- PEPs must include additional information in their 5500 filings, and Forms 5500-SF may be more readily available to PEPs.

Summary of Fiduciary Responsibilities Under ERISA Provisions

- PPP – designated as named fiduciary, plan administrator
  - Responsible for all plan administrative duties to ensure plan qualification and provision of DOL-required disclosures
  - Includes ensuring that employers meet their obligations in this regard
  - Includes ensuring that the ERISA Section 412 fidelity bonding requirements are met
- Trustees
  - Must be qualified to serve as an IRA trustee or custodian
  - May not be an employer
  - Responsible for holding PEP's plan assets
  - Responsible for collecting contributions and implementing "reasonable, diligent, and systematic" written contribution collection procedures

Summary of Fiduciary Responsibilities Under ERISA Provisions (continued)

- Employers
  - Treated as plan sponsors with respect to the portion of the PEP attributable to their respective employees (and beneficiaries), except as to PPP's administrative duties
  - Retain fiduciary responsibility for:
    - Selection and monitoring of PPP and any other PEP designated named fiduciary; and
    - Investment and management of portion of plan assets attributable to their employees (limited exceptions)
    - Query – to what extent can/will employers delegate these responsibilities?
  - Co-fiduciary liability – not specifically addressed – presumably would still apply
- DOL – authorized to perform audits, examinations and investigations of PPPs

Upcoming Guidance

- The SECURE Act directs the IRS to issue appropriate guidance, including guidance:
  - To identify the administrative duties and other actions required to be done by the PPP.
  - That describes the procedures to terminate a PEP and any actions that must be taken by adopting employers when a PEP terminates.
  - That identifies appropriate cases in which the PPP must transfer the assets of employees of an employer that has a qualification failure to an IRA or other appropriate arrangement.
- The SECURE Act directs the DOL to issue appropriate guidance, including guidance:
  - To identify the duties (including the administrative duties) of the PPP.
  - That identifies appropriate cases in which the PPP must transfer the assets of employees of an employer that has qualification failure to an IRA or other appropriate arrangement, and clarifies that such employer (and not the PEP or any other employer) is liable for any liabilities attributable to such employer's employees.

Looking Forward

- The revisions described above are effective for plan years beginning after 12/31/2020.
- The SECURE Act directs the DOL and IRS to issue guidance, but does not include a specific timeline.
  - Until such guidance is issued, PPPs and adopting employers must comply in good faith with a reasonable interpretation of the Code and ERISA.
- Potential PPPs must register with both IRS and DOL before beginning operations as a PPP.
- With all of this to look forward to, how do you tell if a PEP is for you?
- And what issues do we foresee for PPPs, adopting employers, and PEP service providers?

How Does a PEP Differ From a Single Employer Plan?

- Employers have significantly more control over the design and administration of single employer plans than they would over PEPs.
  - Single employer plans come in all shapes and sizes (DB, 403(b), ESOP, etc.)
  - PEP designs are much more limited (DC 401(a), 408)
- But the additional control over the design of a single employer plan comes with additional administrative and, potentially, fiduciary responsibilities compared to PEPs that allow PPPs to handle plan administration.
- PEPs should benefit from significant economies of scale compared to single employer plans.
- PEPs should also benefit from economies of scope, as the PPP will likely have significant retirement plan expertise.

How Does a PEP Differ From a Traditional MEP?

- Traditional MEPs have greater design flexibility (DB, arguably 403(b)), but require commonality among adopting employers.
  - While the commonality requirements have been simplified and relaxed, truly open MEPs are still not permitted.
- As traditional MEPs require commonality, they are likely to have smaller economies of scale.
- But they may have greater economies of scope.
- Employers adopting a PEP may have more limited fiduciary responsibilities, but this does not clearly extend to employers adopting a traditional MEP.

Open Issues for PPPs

- How does a PPP register with the IRS and DOL?
- What are the PPP's duties? What is the best way to fulfill these duties?
- How does one PPP distinguish its PEP from another PEP? Will the PEP allow individual employers to choose from a broad menu of plan design choices through an adoption agreement? Or will it be one-size-fits-all?
- How does the PPP ensure that deferrals are timely remitted into the PEP's trust? If there are delays, is it sufficient that the PPP ensured that the trustee had adequate procedures in place?
- How does the PPP ensure that the PEP's Form 5500 is properly completed?

Open Issues for Adopting Employers

- How does an adopting employer decide whether a PEP is right for them?
- Once they know a PEP is right, how do they decide which PEP to adopt?
- Is the adopting employer's fiduciary liability really more limited than in a single employer plan or traditional MEP? Or is the required PEP language just to reiterate some of the employer's fiduciary responsibilities that apply in any retirement plan arrangement? What about co-fiduciary liability?
- Does the adopting employer need a fidelity bond? What about fiduciary insurance?

Open Issues for Service Providers

- PEPs may induce a large number of small and mid-sized employers into the retirement plan marketplace.
- This could create a significant marketplace for service providers with expertise in PEPs, but also significant competition for existing retirement products and services.
- Trustees servicing PEPs should develop mechanisms to ensure timely remittance of contributions to the PEP's trust.
- Recordkeepers may want to decide between servicing non-recordkeeper PPPs and becoming PPPs themselves.

Everyone into the Pool!

- The SECURE Act generally, and PEPs specifically, may change the retirement plan landscape significantly over the coming years.
- We will keep apprised of developments regarding PEPs, whether they be DOL/IRS regulations, subregulatory guidance, or changes to the marketplace.

QUESTIONS?

Biography

John G. Ferreira represents clients in equity and executive compensation and every facet of employee benefits. He advises global public companies, private equity firms, large financial institutions, nonprofit organizations, middle-market companies, individual executives, and emerging information technology and life sciences companies. John counsels these clients on compliance with ERISA, tax, securities, and labor laws. He also advises vendors to employee benefits plans on compliance with the reporting, fiduciary responsibility, and prohibited transaction requirements of Title I of ERISA. John serves as the managing partner of Morgan Lewis's Pittsburgh office.

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Biography

Daniel R. Kleinman advises businesses on the fiduciary responsibilities provisions (Title I) of the Employee Retirement Income Security Act (ERISA). He also counsels these clients on related tax, corporate, and securities laws in connection with the structuring and marketing of investment products (including private equity and hedge funds) and financial services to employee benefits plans. Additionally, Daniel handles issues related to the regulation of broker-dealers and investment advisers under US federal and state securities laws.

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Biography

Michael B. Richman counsels clients on the fiduciary responsibility rules under the Employee Retirement Income Security Act (ERISA), including the ERISA prohibited transaction rules. He advises plan sponsors on investment matters for defined benefit and defined contribution plans. He also counsels banks, investment adviser firms, and broker-dealer firms on ERISA compliance for ERISA plan separately-managed accounts, collective investment funds, private funds, and other arrangements. Additionally, he provides guidance to IRA custodians on permissible IRA investments and investment restrictions.

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Biography

Michael Gorman advises multiemployer benefit funds, public and private companies, tax-exempt organizations, and governmental employers on the design, governance, operation, and compliance of qualified and nonqualified retirement plans and welfare benefit plans. Mike also counsels clients on legal issues arising under ERISA, the Internal Revenue Code, the Affordable Care Act, the Multiemployer Pension Protection Act, the Pension Protection Act, the Multiemployer Pension Reform Act, HIPAA, and COBRA. Prior to joining Morgan Lewis, Mike worked at a boutique law firm in Washington, DC, focusing on compliance issues confronting multiemployer plans.

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