VOL. 30, NO. 4 WINTER 2017

BENEFITS LAW JOURNAL

Multiple Employer Plans: An Overview of Legal, Regulatory, and Plan Design Considerations for States

David E. Morse and Angela M. Antonelli

Americans are facing a retirement crisis. The foundation for building a secure retirement—Social Security, employer-provided pensions, and personal savings—has been weakened for a number of reasons including that most private companies no longer provide pension plans for their employees,[1] *and employees have*

David E. Morse is a partner in the New York office of K&L Gates, where he is actively involved in the legal and practical issues facing states wishing to establish multiple employer plans, auto IRAs, and other retirement programs for the private sector. In addition to advising a number of states, he is a frequent commentator on the ERISA, tax, and securities laws implications of state initiatives. He has served as editor-in-chief of *Benefits Law Journal* since 2002 and is a fellow of the American College of Employee Benefits Counsel.

Angela M. Antonelli is a research professor and the executive director of the Georgetown University Center for Retirement Initiatives at the McCourt School of Public Policy. She is a fellow of the National Academy of Public Administration, a former federal assistant secretary/chief financial officer and a certified government financial manager.

The views set forth herein are the personal views of the author and do not necessarily reflect those of the law firm with which he is associated. This article was originally published by the Georgetown University Center for Retirement Initiatives and is reprinted with permission.

not saved much on their own for their retirement.[2] *In the absence of federal action, states are leading the way and transforming the retirement savings landscape. Since 2012, at least 40 states have introduced legislation to either establish a state-facilitated retirement plan or study the feasibility of establishing one for private sector workers. Nine states have enacted legislation to expand access to retirement savings plans.*

Although several of these states have enacted individual retirement accounts (IRAs), states have other defined contribution (DC) options, including multiple employer plans (MEPs). These more regulated retirement plans allow for higher levels of savings and employer contributions and represent an alternative that can function alone or with an auto-IRA or other state-facilitated program.

This article provides an overview of how the Employee Retirement Income Security Act (ERISA) and the Internal Revenue Code, as well as securities and other laws, would apply to a state-facilitated MEP.

The deterioration of the foundation for retirement security is one of the greatest economic and financial challenges facing our nation today. Social Security was never meant to be the sole source of income for retirees. Yet Social Security accounts for at least half of total retirement income for more than 60 percent of recipients and over 90 percent of income for more than a third of recipients.[3] According to the US Government Accountability Office (GAO), the overall median balance for working, prime-age households with a DC account in 2013 was $41,900.[4] As of December 2016, the average monthly Social Security benefit for a retired worker is $1,380,[5] enough to place the worker only about 30 percent over the poverty level.[6]

American workers should have easy access to simple, low-cost ways to save, and look forward to a level of financial security in their retirement. The ability of more workers to improve their retirement readiness is made challenging today because more than half of all private sector workers—approximately 55 million Americans—do not have access to retirement savings programs through their employer.[7] Workers are 15 times more likely to save for their retirement if they have a way to save through an employment-based plan.[8]

Small businesses account for approximately two-thirds of workers without access to retirement plans.[9] Small employers recognize that a lack of retirement security hurts business and the overall economy; however, many of them are overwhelmed by the number of plan options, plan legal and administrative requirements and paperwork, and fiduciary responsibilities, such as selecting investment funds and managing plan assets.[10] Moreover, small business owners indicate that cost is the biggest barrier to offering a retirement savings plan.[11] Thus, many private sector employees are left without access to the simplest ways to save for retirement, and they do not take any steps to begin saving on their own.

Most Americans agree that the country's retirement system is under stress and in need of reform.[12] For several years, the White House and Congress have failed to act on legislative proposals to establish new retirement savings programs to close the access gap among private sector workers.[13] Because of the potential budgetary and economic consequences of this failure to address the deterioration of retirement savings for millions of US workers and their families, states have begun to develop retirement savings options for private sector workers.

States are transforming the retirement savings landscape. Since 2012, at least 40 states have introduced legislation to either establish a state-facilitated retirement plan or study the feasibility of establishing one. Nine of these states—California, Connecticut, Illinois, Maryland, Massachusetts, New Jersey, Oregon, Vermont, and Washington—have enacted legislation to expand the accessibility and effectiveness of retirement savings for private sector workers.[14]

New and innovative public-private partnerships are being tested by the states. Several states have established IRAs using auto-enrollment or "auto-IRAs" (California, Connecticut, Illinois, Maryland, and Oregon) or adopted marketplaces (Washington and New Jersey), but Vermont recently became the first state in the nation to pass legislation establishing a multiple employer plan (MEP).[15] A MEP is a single retirement plan adopted by two or more unrelated employers. But what are the legal and regulatory considerations in establishing such a plan, and how does it differ from an auto-IRA plan?

MEPs are covered by ERISA, Tax Code "qualification" rules, and other federal laws. ERISA was passed in 1974 and is administered by the US Department of Labor (DOL) to protect participants and beneficiaries in private sector employee benefit plans, including defined benefit (DB) and defined contribution (DC) retirement plans. ERISA exempts federal, state, or local governmental plans;[16] however, a retirement plan created or operated by a government for private sector employees would not be considered a governmental plan. A state could not escape ERISA regulation simply by bringing private sector workers into its own retirement system.

Although much of the policy discussion to date has been focused on auto-IRAs designed to be exempt from ERISA, IRAs are limited by the lack of employer contributions and lower individual contribution ceilings. MEPs are ERISA-regulated plans allowing for higher levels of savings and employer contributions, and they are an alternative that can function alone or with an auto-IRA or other state program.

WHAT IS A MEP?

A MEP is a "pension plan" covered by the full scope of ERISA and the Tax Code "qualified" plan rules. As a single plan, all MEP assets are pooled to pay the benefits and cover costs.[17] In other words, all participants "eat from the same pot."

A MEP would be a 401(k), that is, a specialized employer DC retirement plan to which employees may make tax-deductible contributions from their wages. A 401(k) is an ERISA-covered retirement plan. Contributions are typically invested by the employees from a menu of investments selected by the employer. Employers also may make contributions into employees' accounts. The employee contribution limits are much higher for a 401(k) than an IRA. If the plan permits, participants may make Roth 401(k) contributions. The plan also may allow employees to borrow from their account. A MEP also may allow preretirement withdrawals but, as with an IRA, tax penalties may apply.

MEPs predate ERISA and the current Tax Code. In the early days, most MEPs were DB plans. Since 1989, when the funding rules changed to essentially make each employer responsible for the underfunding of the other participating employers, virtually all MEPs have been 401(k) and other DC plans.[18] The Internal Revenue Service (IRS) and DOL appear to have different views on what it takes to be a MEP. The IRS has ruled that the combined plan of unrelated employers is a MEP if the program's assets are combined in one pool, without any employer-by-employer segregation.[19]

Technically, because the MEP is considered a single plan, all plan assets are available to pay plan creditors. With a 401(k) or other DC plan, each participant's benefit is held in an individual account and, unlike a DB plan, there is no possibility of unfunded liabilities. Therefore, the pooling of all assets should not put any participant's account at additional risk from fraud, mismanagement, or other incompetent or nefarious behavior by other employers or participants. Importantly, pooling the assets of numerous small and midsized employer 401(k) programs should allow the MEP to accumulate sufficient assets to negotiate lower investment, recordkeeping, and other fees.

However, the DOL has had an extra requirement for MEPs: Unrelated employers can maintain a single plan only if they "are tied together" by "a genuine economic or representational interest."[20] Whether a group of employers is sufficiently tied in an "affinity group" is not mentioned in ERISA as a MEP requirement.

What a MEP Is Not

MEPs are sometimes confused with other retirement plans. A MEP is not a multiemployer plan (a retirement plan established under one or more collective bargaining agreements for unionized workers that is jointly administered by the union and employer representatives). A MEP also is not a single plan maintained by related employers in the same "controlled group" of companies. And a MEP is not a collection of separate plans of unrelated employers that have commingled their plans' assets for investment and recordkeeping purposes.

Federal Guidance Opens MEPs for States

On November 18, 2015, the DOL released Interpretive Bulletin 2015-12[21] relating to state savings programs that sponsor or facilitate savings options for private sector workers through ERISA-covered MEPs, master and prototype plans, and marketplaces. As outlined in this guidance, a government-sponsored MEP enjoys greater operational freedom than one sponsored by a private sector entity. Specifically, a MEP sponsored by a state or local government may allow any business employing state residents to join the program. These so-called "open" MEPs would allow, for example, a state to create a unified program available to all employers. Throughout this analysis, it is assumed that any state-facilitated MEP would be open.

Under a state MEP, each employer that participates would not be considered to have established its own ERISA plan; rather DOL would consider this arrangement a single ERISA plan.[22] Therefore, the state would have economies of scale in lowering administrative and other costs. A single trust would hold contributions made by participating employers, the employers' employees, or both. The state, or designee, would be the plan sponsor and named fiduciary and plan administrator for administering the plan and could contract out to private sector providers to do so.

Employer participation in a state open-MEP must be voluntary. However, its plan design features can include the use of auto-enrollment and auto-escalation.

Establishing a State MEP

A MEP must have a plan sponsor,[23] which could be the state itself but is more likely a board, committee, or other entity appointed or created by the state through enabling legislation.[24] For convenience, this discussion will use the term "board" to refer to all government-appointed administrators. The board would set the program's terms, prepare plan documents, select investments, and hire trustees, custodians, recordkeepers, and other service providers. Employers would voluntarily join the MEP by signing an adoption agreement.

HOW DOES ERISA APPLY TO A MEP?

As previously noted, a MEP is an ERISA retirement plan. To some, ERISA coverage conjures up visions of onerous fiduciary obligations and unlimited liability. ERISA does have a lot of rules, but it also provides workable standards for running a retirement program, a sound set of participant protections, and a well-established system for resolving disputes over benefit claims. ERISA offers a well-established body of law for operating the plan and useful guidance for handling other people's money.

This section provides an overview of how ERISA as well as other laws, such as tax and securities laws, would apply to a MEP. There are ERISA rules on establishing and maintaining a plan; fiduciary duties; federal government reporting and participant disclosure; and when, where, and how a participant or fiduciary can sue for unpaid benefits or harm to the plan. There also are additional considerations applicable to a state-facilitated MEP arising because the state, or its delegate, will assume many responsibilities on behalf of all participants.[25]

Establishing and Running a Plan

An ERISA retirement plan is established by a "plan sponsor" and operated under the terms of a written plan document.[26] Besides setting how benefits are determined and when they vest and are paid, an ERISA plan must designate one or more individuals, a committee, or an entity as the "named fiduciary"—the point person responsible for the other fiduciaries. The document also describes who may amend the plan and may provide for the delegation of authority by the fiduciaries to others. With a state-facilitated MEP, the board, committee, or other special purpose entity designated by the legislature likely would serve as sponsor and named fiduciary and be authorized through enabling legislation to make certain plan amendments. All plan assets (employee and employer contributions and investment earnings) must be held in a trust or in an insurance company annuity.[27] Plan assets are sacred and bulletproof—they may only be used to pay benefits or to cover legitimate plan expenses. Each plan must maintain a fidelity bond.[28]

Fiduciaries and Their Duties

Besides the plan sponsor, named fiduciary, and trustee, anyone with control over plan assets is a fiduciary. This includes a money manager or anyone with responsibility to appoint or fire a money manager.[29] A person who is performing ministerial duties is not a fiduciary.[30] Examples include most recordkeepers, lawyers, and other advisors. A person can wear two hats, serving in both a fiduciary and nonfiduciary role. For example, when a plan sponsor establishes or amends a plan, this generally is a "settlor" decision outside of the fiduciary rules.

Fiduciaries are expected to be experts and to act prudently for the exclusive benefit of participants.[31] ERISA recognizes that not every fiduciary will be an expert, so fiduciaries may instead hire experts to advise them or delegate certain duties to an expert. Hiring or delegating to an expert is itself a fiduciary act. Neither perfection nor clairvoyance is expected of ERISA fiduciaries, just prudent and well-thought out, reasonable decision-making. In the words of a famous judicial opinion, "prudence not prescience" is required.[32]

The plan sponsor and named fiduciary sit at the top and are ultimately accountable for what goes wrong. Under the ERISA concept of prudence, if these fiduciaries are diligent in hiring and monitoring consultants, money managers, trustees, and the like, then they will not have violated their ERISA fiduciary duties even if one of their delegates acts imprudently.

Special Investment Consideration

A large portion of fiduciary efforts concerns the investment of plan assets, especially for 401(k) and other DC plans. ERISA allows fiduciaries to offload much of their fiduciary responsibilities by allowing participants to invest their own plan accounts.[33] For this to happen, participants must be given a choice of at least three diversified investments funds—say an S&P 500 fund, an international fund, and a fixed income fund—the opportunity to switch investments at least quarterly and, of course, proper disclosure to participants. With daily valuation and a dozen or more funds, it is relatively easy for most plans to meet this so-called 404(c) exception. For participants who do not make any investment election, most likely those who were auto-enrolled in the plan, the participant may be "defaulted" into a diversified lifecycle, assets allocation, or similar all-in-one fund.[34] Importantly, although participants can be made legally responsible for their own investment choices, the plan fiduciaries remain responsible for selecting and monitoring the investments offered on the fund lineup and ensuring that the fees paid by participants are reasonable. Another advantage of a state-facilitated 401(k) MEP plan is that by combining many small and midsized employer plans, the program will achieve significant economies of scale, thus lowering participant fees and expanding the available universe of money managers and advisors. These advantages will assist state and employer fiduciaries in fulfilling their obligations.

Reporting and Disclosure Requirements

Each plan must file an annual report (Form 5500, 5500-SF, or 5500EZ) with the IRS each year that includes a financial statement and other investment information and a representation that the plan did nothing illegal. Plans with fewer than 100 participants may file simplified annual reports and are not required to have an outside audit. One advantage of a state-facilitated MEP is that a single Form 5500 and annual audit covers the entire program; adopting employers are spared filing their own reports.

The ERISA disclosure obligations include giving participants a readable "plain English" summary plan description (SPD), a notice of plan amendments (summary of material modifications or SMM), and information on plan fees, investments, and payroll withholding.[35] Participants also must be given a quarterly benefit statement. The good news is that most recordkeepers have fully automated the process, and it should not present an undue burden for state-facilitated plans. Many plans now add simple one- or two-page readable information sheets to the ERISA disclosure so participants have accessible information.

Benefit Disputes and Litigation

ERISA offers a well-developed system for resolving participant disputes. Before suing, a participant must make a benefit claim, have the claim denied by the plan, appeal the denial, and have the appeal also denied.[36] Only then may the participant sue and only in federal court.[37] The appeal/denial process must be in writing, and participants must be given notice of their rights and an explanation of the denial and what other information might be needed to prove the claim. The participant has a right to all relevant plan documents that relate to the claim. The plan may specify a reasonable statute of limitations for making a claim and bringing a lawsuit; otherwise, the analogous state statute governs. A court may award legal fees to either party, but absent outrageous conduct by the participant or counsel, the employer or plan is unlikely to be awarded fees. However, a court may award fees to a losing participant, if the participant had “some degree of success on the merits.”[38] A plan may provide that all disputes be litigated in a particular jurisdiction; for example, a Vermont-based plan could limit litigation to the courts in Vermont.

If the plan suffers a loss, for example, due to fraud or negligent action by a money manager, the fiduciaries may sue on the plan’s behalf. Again, the suit must be in federal court. Courts generally have not required participants to exhaust administrative remedies before suing for breach of fiduciary duty.

Prohibited Transactions

ERISA (and the Tax Code) penalize certain “prohibited transactions” between a plan and a related party.[39] These transactions include the direct or indirect sale or exchange, leasing of any property, lending of money, or supplying goods and services between the plan and party in interest. Fiduciaries are obligated to make sure the plan avoids these transactions. Fiduciaries also must avoid self-dealing or taking actions that are averse to the plan. (There are numerous statutory and DOL-issued exemptions to these prohibited transactions.) Illegal transactions must be reversed, the plan made whole, and a penalty paid by the related parties.[40]

Special ERISA rules cover a plan’s investment in employer stock.[41] In virtually all cases, the employers joining a state-facilitated MEP would be privately held, so it is unlikely that these rules would ever be implicated. Nevertheless, the program should screen its employers and have appropriate notification and other investment procedures in place in case an employer is or goes public.

HOW DOES THE TAX CODE APPLY TO A MEP?

Like any retirement plan, MEPs enjoy various federal income tax benefits. For example, employer contributions are deductible when made, the plan does not pay income taxes on its investment income, and participants defer any taxation until they receive payment. Also, upon leaving a job, participants may be able to rollover their benefits tax-deferred into an IRA or new employer plan. To achieve these tax advantages, a MEP must be “qualified” by meeting numerous Tax Code requirements, which boil down to a series of rules, mathematical formulas, and limits that are intended to keep the plan from favoring highly compensated employees (HCEs) too heavily, limiting preretirement access to funds, or delaying distributions too long. What follows is a brief synopsis of these rules.

The IRS is responsible for interpretation and enforcement of the Tax Code.

Some of the Tax Code rules apply to the MEP as a whole, and others apply to each employer individually. This distinction can be quite significant and will be appropriately indicated in each following section. (Note that the plan vs. employer difference generally does not have a practical impact in applying the ERISA rules.)

Nondiscriminatory HCE Eligibility

Basically, an HCE is any employee who is (or was in the prior year) a 5 percent owner or was paid $120,000 (indexed for post-2017 inflation) in the prior year.[42] Whether an individual is an HCE and the plan discriminates is determined employer by employer.[43]

All employees who are not highly paid are considered non-highly compensated employees (NHCEs). The plan must cover a reasonable percentage of NHCEs; for example, a plan benefiting 70 percent of NHCEs would pass "coverage."[44]

Certain employees, such as those with less than one year of employment, part-timers who never work 1,000 hours in any year, individuals under age 21; and unionized employees (if retirement benefits were considered during collective bargaining), may be excluded in coverage testing. Other categories of employees must be counted in coverage testing but may be excluded from the plan—such as based on job function or location, as long the plan still meets the 70 percent or similar test.

Presumably, most state-facilitated MEPs would require that each employer cover all employees, perhaps after a short waiting period. Thus, passing the coverage test should be simple. Only employees and owners working for the business may participate in the employer's plan. Although a business's nonemployee consultants and other independent contractors cannot participate in that business's plan, they could set up their own retirement plan as a self-employed worker.

Service with Any Participating Employer

Employment with any employer participating in a MEP must be counted in determining whether an employee satisfies the plan's age, service, and vesting requirements.[45] This rule would help workers who job-hop between participating employers from forfeiting nonvested benefits or having to meet multiple waiting periods. It should be relatively simple to track employees through their Social Security numbers.

Nondiscriminatory Benefits and Features

The Tax Code limits the amount of an employee's compensation that may be considered in figuring the employee's 401(k) and employer contributions to $270,000 in 2017 (indexed for inflation). The annual contribution added to an employee's account (both 401(k) and employer) in 2017 may not exceed $54,000 or 100 percent of compensation, whichever is lower.[46]

Besides coverage, the plan's benefit structure and other important features generally must treat all participants the same. It is possible for a plan to offer different benefits to various categories of employees—for example higher employer contributions for workers with at least ten years of employment. However, the more generous provisions must be able to pass the coverage test as if it were a distinct plan. Oddly, compensation limits are applied employer by employer while the contribution limits are applied plan-wide. For example, if someone is employed by two participating employers, his or her contributions by both employers are added together.[47] Again, as a practical matter, most state-facilitated MEPs would require that each employer offer the same benefits to all its participants, so the plan should automatically be nondiscriminatory.

Contributions

Employers may contribute to each participant's account under a stated "allocation formula" and within the limits discussed. Employer contributions can be discretionary—the employer decides at year-end whether and how much to contribute—or hard-wired into the plan document. Even hard-wired contributions can be changed or eliminated prospectively.

It is also possible for an employer to contribute disproportionally more for employees earning above the Social Security wage base ($127,000 in 2017). The rules for "integrating" a plan with Social Security are complex. For these reasons, states should use caution in considering an integration option. Finally, a plan may permit employees to make after-tax contributions to the plan. As discussed later, given the advantages and relatively high limits of traditional and Roth 401(k) contributions, most state-facilitated MEPs probably would not allow after-tax contributions.

Exclusive Benefit Rule

Every plan must be established and maintained by an employer for the exclusive benefit of its employees and their beneficiaries.[48] The

IRS interprets the exclusive benefit rule as generally requiring that all covered employees must be employed by the employer or employers maintaining the plan.

The exclusive benefit rule applies to the entire plan.[49] Although the state sponsor will not have any employees participating, the requirement should be satisfied because all employers will adopt the plan and delegate to the board responsibility for running the plan.

An analogous issue arose some 20 years ago, regarding whether leased employees could participate in the leasing company (sometimes called a professional employee organization or PEO) 401(k) plan. The PEO typically treated the leased workers as its employees and not as employees of the company they were being leased to. But labor law can be unclear as to who employs them. To allow the PEO plan to cover these employees no matter whom was considered their employer, the IRS ruled[50] that a PEO plan should be converted into a MEP covering all leased employees, with the recipient businesses adopting the MEP. Thus, the exclusive benefit question will be solved even if the workers were determined not to be employees of the PEO. Similar logic should prevail regarding a state-facilitated MEP, because each employer would adopt the plan as a condition of joining.[51] Nevertheless, before proceeding, a more cautious state may wish to obtain guidance from the IRS.

General Operations

Every plan must be operated in accordance with its written terms, unless the terms themselves are illegal. Both employee and employer contributions must be made on time, accurately, and as specified in the employee elections and plan document. Noncompliance with either of these rules also would be an ERISA violation.

Top-Heavy Rules

The Tax Code imposes an extra layer of requirements on mostly small employers with plans that are stacked too heavily in favor of "key" employees, defined as 5 percent or greater business owners, one percent owners earning at least $150,000 (indexed), and certain officers and other "high-paid" employees.[52] If more than 60 percent of the account balances are held by key employees,[53] the plan is "top-heavy" and must either provide minimum benefits to non-key employees or contribute at the same rate for all employees. Top-heavy plans also must use a slightly faster vesting schedule.[54] The top-heavy rules apply employer-by-employer.[55]

Although a MEP would have to test each employer for top-heaviness, most state-facilitated plans would have uniform contribution rates and fast or immediate vesting that would automatically satisfy this rule. Also, a plan meeting the special 401(k) testing rules (the so-called ADP/ACP safe harbor) would satisfy the top-heavy rules.

Vesting

Participants always are 100 percent vested in their own 401(k) and after tax contributions.[56] The plan may impose one of two vesting requirements on employer contributions: Either contributions are 100 percent vested when the employee has three years of service with the employer, or they vest gradually—20 percent per year for each year of service starting with the second year, so that the employee is 100 percent vested after six years.[57] Of course, a plan may use a faster (more generous) vesting schedule. Each employer could be allowed to choose its own vesting, but as a practical matter, states will want to hard-wire the vesting schedule into the plan document.

Generally, all service with any employer participating in the MEP counts for vesting purposes.[58] Employees also vest upon reaching the plan's stated retirement age (generally age 65) while employed.[59] If an employee leaves before full vesting, the employee will forfeit the nonvested benefits. Forfeitures may be used by the employer to reduce future contributions, pay plan expenses, or as an additional contribution for the remaining participants.[60] How forfeitures will be used should be clearly specified.

Spousal Rights

A DC plan participant must designate the participant's spouse as sole beneficiary unless the spouse consents in a notarized writing to waive this right.[61] Upon divorce or legal separation, a court may issue a domestic relations order to the plan ordering it to transfer a specified portion (or even all) of the participant's benefit to a plan account set up for the spouse. These spousal rights can get rather complicated, but many recordkeepers have well-established systems to take charge.

Loans, Withdrawals, and Distributions

The Tax Code permits a plan to allow participants to borrow from their account. The maximum loan is the lesser of $50,000 or 50 percent of the vested account. Loans may extend up to five years (longer if used to purchase a primary residence) and must charge a "commercially reasonable" interest rate. Interest and principal payments (typically through payroll withholding) are returned to the participant's account.

Although better than credit card, payday, and some other forms of consumer credit, loans are not a particularly good deal for participants. Generally, the interest on the loan is not tax deductible but will be taxed upon distribution. Thus, loan interest is paid with after-tax dollars but is taxed (again) on retirement. More important, a significant minority of participants default on their loans, causing the balance of principal and accrued interest to be immediately taxed and possibly triggering a 10 percent IRS early withdrawal penalty as well.

A plan may allow participants to withdraw money from their vested account while employed. Typically, these withdrawals are limited to an IRS list of financial hardships. Examples of hardship include the purchase of a home, college and other post-high school educational costs, to prevent foreclosure or eviction, and funeral expenses. The rules on withdrawal are considerably stricter for 401(k)s than most employer contributions.[62] Withdrawals are taxable and generally hit with the 10 percent early withdrawal tax. Earnings on 401(k) contributions may not be withdrawn for hardship. A plan may allow withdrawals from employer contributions, with or without hardship and from all contributions, once the participant reaches age 59-1/2.

Although most plans allow loans and hardship withdrawals, these features can be problematic. Number one is that easier access to 401k) funds can cause "leakage"—spending money earmarked for retirement on day-to-day expenses. Also, although recordkeepers have largely automated the process, they still add to expenses and headaches and are error-prone. Conversely, the availability of loans and withdrawals may lead some folks to contribute (or contribute more) knowing that they'll have access to the money just in case. A plan may impose a reasonable fee on participants taking a loan or hardship distribution. States should give serious thought to limiting employees' access to money before retirement.

When an employee retires or otherwise leaves employment, the employee may choose when and how to take payment within the alternatives allowed by the plan. Although a plan could only offer lump sums, most states would want to allow installment and annuity payouts and give participants the ability to defer distribution if the Tax Code allows.[63]

The state may nudge participants into taking at least a portion of their benefit as a lifetime annuity. For example, a MEP could provide that the "normal form" of payment is a lifetime annuity (with spousal survivor benefits) from an insurance company and that retirees must affirmatively choose a lump sum or installment payments. Choosing the insurance company is a fiduciary decision of the state sponsor or its delegate.

An employee leaving one employer participating in a MEP for another MEP employer probably would not be considered to have terminated employment.[64] The plan must begin distributions to a participant when he or she reaches age 70-1/2. However, an employee, other than someone with a 5 percent or greater interest in the business, may delay these minimum distributions until actual retirement. As discussed later, the age 70-1/2 rule also does not apply to amounts held in a Roth 401(k) account.

ADDRESSING MISTAKES, VIOLATIONS, AND LIABILITY

All plan sponsors should have procedures in place to prevent, catch, and remedy mistakes and violations and allocate financial responsibility to the guilty. This is an issue for a MEP where the state, as sponsor, will need to take the lead. State legislatures should have their eyes open to these issues, but it should not dissuade them from establishing MEPs.

For participating employers, an important advantage of joining a MEP will be significantly reduced liability exposure compared with operating its own single employer plan. By following well-worn ERISA governance procedures and principles of transparency and outsourcing most functions to vendors, states and employers can, as a practical matter, avoid most liability.

Late 401(k) Contributions

Employers have a duty under both ERISA and the Tax Code to properly withhold and transmit 401(k) contributions. The DOL has a focus on late 401(k) contributions, viewing them as, in effect, interest-free loans to the employer. Although there is no statutory standard for when a contribution is late, the DOL has established a deadline rule that 401(k) contributions must be delivered as soon as they reasonably can be segregated, but no later than the 15th business day of the month immediately following the month in which the paycheck was issued. (The DOL gives an automatic pass to plans with fewer than 100 participants if contributions are made within seven business days after issuing the paycheck. It is not clear whether this small-plan exception would apply to small employers in a state-facilitated MEP where the plan, but not the employer, had over 100 participants.)

One way to judge how fast an employer could reasonably segregate its 401(k) contributions is to look at how quickly an employer can forward tax withholdings to the IRS. The contribution timing rule also applies to loan repayments made through payroll.

Smaller employers, perhaps using an outside service but still relying on a multitasking employee to manage payroll, can find this rule challenging. Recognizing the difficulty, the DOL has created a correction program that allows offending employers to add an interest factor (calculated on the DOL Web site) to each employee's late contribution. An employer's occasional violation can be self-corrected, while more frequent problems should be reported using the DOL voluntary correction program. Of course, chronic lateness or fraud are serious violations that could lead to penalties and other sanctions.

Late contributions should be viewed as an employer issue that the state sponsor is neither able to police nor remediate. The MEP plan documents should make this clear. As open 401(k) MEP coverage grows, states, employers, the DOL, and IRS will likely develop additional solutions.

ERISA Fiduciary Concerns

The state board can, and should, hire investment advisors and recordkeepers to accept responsibility for the heavy lifting of investing and operating the plan and agree to indemnify the board if something goes amiss. Of course, the board still would retain its ERISA duty to locate, hire, monitor, and replace (if necessary) those vendors.

The board should retain expert consultants and attorneys to help with these duties. Recall that ERISA does not impose a duty of perfection and, by having and following proper procedures and governance, a board would generally be absolved from liability if one of those vendors turned out to be a loser. Indeed, most states already have in place detailed request-for-proposal and contracting rules to manage the process; the enabling legislation establishing the MEP could designate the extent to which state procurement rules (or a more flexible approach) should apply to the selection of investments and vendors.

A board could purchase fiduciary insurance to further mitigate its exposure. That insurance should be purchased with outside (and not plan) funds. Otherwise, any insurance recovery would belong to the plan. Everything considered, the combination of outsourcing, indemnification, sound governance, outside experts, and fiduciary insurance should allow even the most nervous board member to sleep at night.

One exposure for ERISA liability that cannot be outsourced or insured away is for the board's own fraud, malfeasance, or complete abdication of duties. But there should be plenty of checks, balances, outside auditors, and procedures to prevent this type of abuse.

From the employers' side, joining and remaining in a MEP are considered fiduciary decisions. The potential ERISA liability from an employer's participation in a state-facilitated MEP, backed by a team of experts and seasoned providers, would seem almost illusory.

Mistakes, Corrections, and 'Bad Apples'

Violation of any of the Tax Code requirements could, in theory, cause any plan, including a MEP, to be "disqualified." Disqualification is the IRS's nuclear option, causing the plan to retroactively lose all favorable tax benefits, immediately taxing participants on their vested benefits even if not paid out, the plan to pay income tax on its investment earnings, and the employer to lose some of its tax deduction on contributions, plus interest and tax penalties imposed on everyone.

Under the controversial "bad apple" rule, the IRS treats one employer's violation—for example, of the top-heavy or 415 benefit limitations—as infecting the entire MEP.[65] Due to the draconian consequences, the IRS is loath to disqualify a plan. Instead, it has created a series of procedures by which an employer can correct a qualification defect.[66] Depending on the relative size and nature of the error and how it was caught (by the employer and self-corrected and reported, or by the IRS on audit), almost all errors may be fixed by undoing the mistake, making all participants whole and, perhaps, by the employer paying an IRS user fee or penalty.

In a MEP, the plan administrator (not the employer that messed up) must orchestrate the correction and apply for IRS relief.[67] The administrator may allocate any IRS compliance fee or penalty to the offending employer or employers, rather than to all employers. A well-designed MEP would include procedures for identifying and correcting mistakes, allocating the costs of correction, and authorizing the administrator to compel the employer or employers to fully cooperate and assume financial responsibility for its noncompliance.

Even with the correction procedures and the important policy goals of a state-facilitated MEP, some states and employers may not feel entirely comfortable relying on the common sense and good graces of the IRS in correcting errors. Although careful plan design can reduce the likelihood of a qualification error and make the offending employer pay for its own mistakes, the bad apple rule may be the most troubling aspect of joining a MEP.

It also does not serve any regulatory purpose to punish the innocent along with the guilty. Either the IRS should revise its policy, or Congress should pass legislation repealing the bad apple rule. Until then, the bad apple rule could be a factor in a state's decision to take a different approach; avoiding one problem at the possible cost of forgoing the many advantages of a MEP.

MEP PLAN DESIGN AND OPERATION: FREQUENTLY ASKED QUESTIONS

In considering whether to adopt a MEP, there are some additional questions related to a plan's design, features, and operations that may be taken into consideration.

Do Employers Have Flexibility with Plan Features?

Although the Tax Code is silent, it should be possible for a MEP to permit employers to choose different contribution rates or other plan features from a menu of terms established by the board. Any alternatives should balance employer preferences against administrative costs and complexity. For example, to avoid any nondiscrimination violations, an employer could be required to apply any selected contribution or other feature to all of its employees. Alternately, a state may wish to eliminate most flexibility, say by requiring auto enrollment, safe harbor matching contributions, and 100 percent vesting. No matter what, states should not give employers any choice over investments.

What Are Options for Paying for Plan Operations?

Most, if not all, states will want the MEP to cover the cost of its own operations. This would include not only recordkeeping and investment fees but also expenses for outside lawyers, consultants, auditors, and employee education and communication. Each employer could be charged for its share of some or all of these expenses, but DC plans typically impose these costs on participating employees. Employee payments can be handled through fees embedded in mutual fund and investment management fees or by a separate charge (percentage or flat fee) deducted from each employee's account. The trend among larger, more sophisticated plans is to only embed investment-related fees and separately charge for all other expenses. To avoid undue hardship and the chilling effect of a flat-dollar fee on new and low-paid employees but without penalizing long-tenured high savers, a plan could charge a percentage fee up to a stated cap.

State-facilitated MEPs raise two additional fee questions: Who pays the start-up costs, and can participants be charged for "settlor-type" expenses? First, to the extent that start-up costs are not picked up by taxpayers or outside donations, they would have to be covered, as a practical matter, by employees. Obviously, it would be unfair and a likely deal killer to charge newly enrolled employees for their "share" of the start-up costs through higher investment and accounts fees, until these expenses are recovered. And ERISA requires that all charges paid by the plan and participants must be reasonable for the services provided.[68] Thus, the practical solution would be for the recordkeeper to initially absorb these costs as an investment to be recovered gradually through its profit margin. No doubt, each state will take its own approach to this issue.

The second question concerns whether ERISA limits the types of state or board expenses that may be imposed on participants. Under ERISA, participants may not be charged for "settlor" expenses. For typical employer-sponsored plans, settlor expenses involve employer activity for its own (and not the plan's) benefit.[69] Examples include costs of a design study on whether to add a new feature to the plan. However, with a state-facilitated MEP the start-up and other settlor-type costs are incurred by the state, not the employer.

Logic dictates that these state expenses are not the type of settlor charges proscribed by the DOL, because the expenses incurred by the state or board are to benefit the plan. After all, the state will not have any employees covered by the plan and will be acting solely to promote retirement savings by private-sector workers. (Of course, this would not be the case if the board abused its authority, for instance, by holding meetings at exotic luxury resorts.) Thus, all expenses should be considered as payable by the plan under ERISA. Given the DOL's stated goal of encouraging states' efforts to promote retirement security, all reasonable board expenses should be payable from the plan. However, states may wish to seek informal or formal guidance from the DOL on this point.

Can an Employer Withdraw from a MEP?

A MEP can (and should) allow an employer to withdraw by "spinning off" the employer's slice of assets and benefit obligations into its newly established plan and trust. Participants' vested and nonvested benefits must be preserved in the new plan. The MEP's administrator would likely have an ERISA fiduciary duty to obtain assurances from the employer that the new plan appropriately treats participant benefits. It also would be possible for an employer to cease (freeze) all employer and employee contributions to the MEP while allowing existing account balances to remain under the plan's regular investment and distribution rules. In that case full vesting of the affected participants' accounts may be required.

Finally, it would be possible for an employer with an existing plan to transfer that plan into a MEP. However, under the existing ERISA and tax rules, any defect in an employer's plan could port over to the MEP, potentially infecting the entire program. It is doubtful an administrator would want to put in the time and expense of due diligence of the employer plan and, absent a change in law, it would be inadvisable for most MEPs to accept a transfer from an existing plan.

Can a State Exit Its MEP?

A state may determine that it no longer wishes to sponsor a MEP—for example, because the retirement plan market has expanded to offer many strong private sector alternatives. In that case, a state would have two alternatives. First, it could find a qualified private sector provider to take over and transfer sponsorship. Of course, this is a fiduciary action and the state would want to obtain airtight indemnification from the new sponsor.

Second, the state could terminate the MEP. This process would involve giving employers the opportunity to set up their own replacement plans and, for the remainder of the MEP, fully vesting all participants;, applying to the IRS for a determination letter that the termination comports with the tax qualification rules, and distributing benefits to all participants. Although a termination would be a cumbersome process, states should be comforted in knowing they have an "out."

Can a State Implement a Program Using Alternative Administrative Structures?

Typically, a MEP would be created through the enabling legislation appointing a board to study, design, and sponsor the plan within specified parameters. This process would be governed by the state's procurement and contracting rules, and the employees hired by the board would be state employees. However, some states may find that some of these rules are unduly restrictive and unwieldy. In that case, and depending on state law, the board could operate through a less regulated nonprofit corporation or similar entity that would provide some flexibility but still be subject to state oversight. Maryland has adopted this approach in the implementation of its auto-IRA program, but it can also be considered for a MEP.

Are There MEP-like Alternatives?

A state could create a program that is in some respects similar to a MEP but is legally a collection of individual plans. Such a non-MEP or pooled retirement plan could provide commingling of investment assets; a single recordkeeper, trustee, and custodian; and a uniform administrative platform for adopting employers. Each employer would have its own plan document, but the state could impose a standard set of contribution, vesting, distribution, and other rules on adopting employers. A non-MEP would avoid the bad apple and special service counting rules (because each plan is completely separate), but each plan would have its own IRS reporting, audit, and disclosure obligations. More significantly, federal securities laws would likely limit investment flexibility to registered products such as mutual funds and make administration more unwieldy and costly and, perhaps, increase employer's fiduciary duties.

How Does Federal Securities Law Apply?

A state-facilitated MEP will commingle and invest program monies—in various mutual funds, group trusts, or in tandem with the state's own pension system. The program should be designed so that these investments are not required to be registered as an investment company or security under the federal securities laws.[70] Ordinarily, this should be relatively simple, because The Investment Company Act of 1940 (40 Act)[71] generally excludes qualified retirement plans from regulation. The Securities and Exchange Commission (SEC) has taken the position that only a single plan—one in which all assets are comingled and available to pay benefits under the IRS rules (*i.e.*, a MEP)—would be exempt. Unfortunately, a few statements by the SEC have suggested that it may view the existence of an affinity group as an additional requirement.[72]

Although a full discussion of federal securities laws is beyond the scope of this article, in certain instances, especially when the plan invests alongside the state pension system, an additional "failsafe" step may be needed to achieve exemption from federal securities laws. For example, a state could use its own banking powers to establish a non-depository trust company to serve as trustee of the plan. The trust would be exempt from the 40 Act and would not need to be registered as a security under the Securities Act of 1933 (33 Act).[73] Significantly, the securities law exemptions only apply to qualified plans; they do not provide relief for IRA arrangements or for commingled investment funds holding IRA assets.

THE CASE FOR MEPS

A MEP offers several advantages for employers, especially smaller to midsized employers, and their employees. First, by commingling assets, a MEP may achieve the economic heft to obtain lower investment and administrative fees, more sophisticated investment opportunities, top-shelf service providers, and such add-ons as financial education and advice. Second, a MEP offers employers a simplified, turnkey process for obtaining a plan document, selecting and monitoring the investment platform and the recordkeeper, IRS reporting, obtaining an independent audit, and similar chores. Finally, by outsourcing most of the heavy lifting to the sponsor and its team of outside experts, employers can significantly minimize their exposure to possible ERISA liability.

Today, small businesses tend to avoid offering retirement benefits because they are too expensive and too time-consuming to manage, and they expose the company to liability if something goes wrong. On the other hand, the economies of scale generated by numerous businesses joining in a single plan should make a state-facilitated program less expensive and the board, with its selected cadre of investment managers, advisors, and service providers, makes the plan more attractive to employers.

Participating employers in a state-facilitated program that is a MEP also should have minimal ERISA fiduciary responsibility (basically whether to join, remain in, or leave the plan) and, thus, minimal liability exposure. In a non-MEP collection of single plans, each employer may be viewed as having greater fiduciary responsibility for plan functions and, thus, greater potential liability. Also, MEPs enjoy exemption from the federal securities laws that could otherwise treat the program as a "security" or "regulated investment company."

There also are several regulatory and cost advantages to being treated as a MEP. As a MEP, one IRS Form 5500 Annual Report is filed, one ERISA fidelity bond purchased, and a single annual audit by an independent accountant conducted for the entire plan.

PLAN DESIGN FEATURES: 401(K)S VS. IRAS

The benefits of ERISA-covered and income tax-qualified plans include higher contribution limits, the ability of both employers and employees to contribute, and numerous service providers experienced in administrating ERISA 401(k) plans. However, ERISA does require participation by employers and employees to be voluntary.[74] This section provides a brief comparison of payroll deduction IRAs and MEP 401(k)s.

Auto-Enrollment and Auto-Escalation

401(k)s. Since the enactment of the Pension Protection Act of 2006, automatic enrollment and automatic escalation have been design features available to 401(k) plans.[75] Using auto-enrollment, a new participant would contribute at a specified default rate unless the participant affirmatively opts out or chooses a different rate. With auto-escalation, a participant's contribution rate is periodically increased by a set percentage, again with ability to opt out or choose a different rate. For example, a plan could auto-enroll participants at 5 percent of pay, and increase the contribution rate by one percent each December 31st after the first year, until the participants reach 15 percent.

IRAs. A payroll deduction IRA also may use automatic enrollment and escalation. Under a 1975 DOL safe harbor, such payroll deduction auto IRAs should not be covered by ERISA.[76]

Auto-enrollment and auto-escalation have been very successful in getting employees, even lower-paid employees, to contribute to a retirement savings plan. Behavioral economists claim these tools help to address the twin forces of inertia and "framing." States should carefully consider where to set the bar and how much flexibility to give participants to adjust their contribution levels. Any state program would not want to unwittingly discourage workers from saving more than they would do on their own by setting the automatic contribution levels too low. The program must also factor in long-term program costs and the need for the program to become self-sustaining within a reasonable amount of time.

Employer Participation

401(k)s. An employer's participation in a MEP or other ERISA-regulated retirement plan must be voluntary.[77]

IRAs. State law could require that certain employers allow their workers to make payroll deduction IRA contributions to a savings program that is exempt from ERISA.

Employer Contributions

A major difference between ERISA-exempt payroll deduction IRAs and ERISA-based 401(k) programs is the ability of employers to make contributions to an employee's account.

401(k)s. Employers can contribute to employees' accounts. An employer also may choose to "match" a portion of each employee's 401(k) contributions. For example, an employer could match participant's

401(k) contributions 50 cents on the dollar up to the first 6 percent. A plan may, but most do not, match age-50 catch-up contributions.

Matching contributions may be automatic (*e.g.*, hard-wired into the plan but amendable prospectively) or discretionary (employer decides year by year). For administrative ease, most states would likely want to limit employer discretion, for example, by specifying the matching formula but allowing employers some discretion to make additional contributions at year-end.

IRAs. Employers are not permitted to make contributions to any payroll deduction IRA. Doing so would establish an employee benefit plan subject to ERISA.

Employee Participation

Employee participation is always voluntary for both IRAs and 401(k)s. If auto-enrollment is used, the employee always has the choice to opt out of participating in the program, and the state would have to determine how much time a worker would have to opt out of the program. A state program also would have to make decisions about how to enroll employees, what information to provide, and the frequency of open-enrollment periods that allow workers to make changes to whether and how much they contribute to their accounts.

Employee Contribution Limits

If a program uses auto-enrollment, another important question is should a default contribution level be set and, if so, at what level. A major difference between ERISA-exempt payroll deduction IRAs and ERISA-based 401(k) programs is the annual contribution limits for workers.

401(k)s. Employee 401(k) contributions are tax-deferred up to the Tax Code's limits—for 2017, $18,000 for those under 50 and $24,000 for those who will be at least 50 by year-end. (Dollar limits are indexed annually for inflation.)

Alternatively, an employee can contribute up to these same limits as post-tax Roth 401(k) contributions. If the Roth contributions are held in the plan for at least five years, then all distributions (Roth plus investment income) are 100 percent tax-free. A plan can give participants a choice between making Roth or traditional 401(k) contributions; the special income limitations on Roth eligibility do not apply to Roth 401(k)s.

It would take a crystal ball to know for certain whether a participant should make a Roth or traditional 401(k) contribution. Roth 401(k)s are advantageous if the participant will be in a higher tax bracket when the participant retires or otherwise withdraws the money; traditional is better if the participant will be in a lower bracket at retirement. If the participant's tax bracket remains the same, then traditional and Roth 401(k)s are generally identical. Given that many participants in a state-facilitated MEP may be relatively low-paid, offering both with Roth as default may be preferable.

Roth and Traditional Contributions

IRAs. Traditional and Roth IRAs contributions cannot be more than $5,500 per year ($6,500 for individuals age 50 and older) or the taxable compensation for the year.[78] Special income limitations apply to Roth IRAs. In general, single taxpayers with adjusted gross incomes above $133,000 in 2017 and married joint filers earning above $196,000 in 2017 (both indexed) cannot make Roth IRA contributions.

- **Traditional IRA:** Contributions may be fully or partly deductible and generally amounts in the account (including earnings and gains) are not taxed until distributed.[79] Required minimum distribution begins on April 1 of the year following the calendar year in which the account holder reaches age 70-1/2.[80]

- **Roth IRA:** Contributions are not deductible and qualified distributions are tax-free.

Contributions are permitted after the age of 70-1/2 and minimum distributions do not apply to employees.[81]

Withdrawal Limitations

Both ERISA-exempt payroll deduction IRAs and ERISA-based 401(k) programs allow for withdrawals from accounts. DOL rules allow states to have control to establish restrictions on withdrawals to limit leakage.[82] The Tax Code does not prohibit early withdrawals; it just imposes a penalty. States are free to add their own early withdrawal limitations, such as a hardship requirement.

401(k)s. Hardship withdrawals are allowed, including for the following:

- Medical expenses for an individual, spouse, or dependents

- Purchasing a principal residence

- Postsecondary education expenses for an individual, spouse, or dependents

- Payments to prevent eviction or foreclosure on a principal residence

- Funeral expenses
- Certain expenses relating to repairs to a principal residence

Generally, withdrawals made before age 59-1/2 are taxed at 10 percent, unless they fall under exceptions.[83]

IRAs. Withdrawals for IRAs vary depending on whether it is a traditional or Roth IRA.

- **Traditional IRA:** Any deductible contributions and earnings that are withdrawn or distributed are taxable. An individual under age 59-1/2 may have to pay an additional 10 percent tax unless the withdrawal qualifies for exceptions.[84]
- **Roth IRA:** There are no penalties or taxes for a qualified distribution (payment or distribution made five years after the first contribution and after age 59-1/2 or due to disability, made to a beneficiary after death, or to meet the requirement of a first home purchase). All withdrawals of contributions are tax-free. An individual before age 59-1/2 may have to pay an additional 10 percent tax on withdrawal of accumulated income unless the withdrawal qualifies for an exception.[85]

COMPARISON OF KEY CHARACTERISTICS OF STATE-FACILITATED IRAS VS. MEPS

The key issues that a state legislature must consider in setting the general specifications for a state-facilitated retirement program include the following:

Program/Feature	**Payroll Deduction IRA**	**401(k) MEP**
ERISA regulation	ERISA-exempt	ERISA-covered
Administrative simplicity	Yes	Yes, but more complicated than an IRA
Employer mandate	Yes, if the program is not an ERISA-regulated retirement plan outside of ERISA preemption	Not permitted
Auto-enrollment with employee opt out	Available	Available
Contributions	• Employee: Yes; both traditional pre-tax and Roth. • Employer: No	• Employee: Yes; both traditional pre-tax and Roth. • Employer: Yes

Investments	Employee chooses from a plan menu, including a state-pooled and professionally managed option or private sector (third-party) options; or the state could choose to direct investments.	Employee chooses froma plan menu, including a state-pooled and professionally managed option or private sector (third-party) options; or the state could choose to direct investments.
Withdrawals and loans	Permitted, but tax penalties would apply. States can have discretion to limit withdrawals to reduce leakage. Loans are not permitted.	Permitted, but tax penalties would apply. States can have discretion to limit withdrawals to reduce leakage. Loans within Tax Code limits may be allowed.
Pros	• Simple • Low-cost • Easier to establish • Can mandate employer participation	• ERISA protections • Some complexity but flexible design • Employees may contribute more up to $18,000 ($24,000 ≥ age 50); • Allows employer contributions
Cons	• No ERISA protections • Relatively low contribution levels of $5,500 ($6,500 ≥ age 50) • No employer contribution • Some participant leakage depending on plan design • Investment risk on participant	• Employer participation must be voluntary • Some participant leakage depending on plan design • Investment risk on participant

FEDERAL MEP REFORM PROPOSALS

There also are several proposals to allow private sector vendors the same flexibility as states to sponsor open MEPs under the commonality rule discussed previously.[86]

CONCLUSION

Congress, the DOL, and the IRS would be welcome to further simplify compliance and mitigate risks to make it even easier for states to sponsor open MEPs. For example, numerous bills have proposed revising the Tax Code to eliminate the bad apple rule for any employer error. There has been general bipartisan support in Congress to make MEPs more user-friendly and address legal concerns.[87]

A 401(k) style MEP with auto-enrollment/auto-escalation would harness a proven formula for helping employees save meaningful amounts for retirement. These programs should garner sufficient assets to achieve economies that would enable small and midsized employers to offer their workers a retirement plan without the costs, fears, and difficulties normally associated with ERISA regulations. Of course, interested states also should support efforts in Washington, DC, to make MEPs an even better retirement savings vehicle.

Too many Americans are finding it increasingly difficult to save for their retirement. The implications for government programs could be significant with a rapidly aging population living longer than ever before with little or no retirement savings. States are leading the way in developing simple, easy-to-use retirement plans to help private sector employees save for retirement. State innovation should be encouraged because every state has unique demographic, economic, and retirement needs. No plan design option is without some uncertainty regarding the way federal employee benefit, tax, and securities laws apply.

Although simpler, lower cost, and easier to establish, IRAs are limited by low contribution levels and no possibility of employer contributions by participants. The state would also have to assume responsibilities for establishing a fiduciary and consumer protection regulatory framework because it would not be subject to ERISA.

To permit larger employee contributions, employer contributions, and generally greater flexibility, a 401(k) DC approach, such as a MEP, would be needed. The plan would be covered by ERISA, but this need not be viewed as an obstacle, although employer participation would have to be voluntary and may reduce overall participation. An ERISA plan can be structured to minimize the possibility of ERISA liability to the state and the program governing board, be user-friendly to adopting employers, and offer employees the added protections that ERISA provides.

NOTES

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12. Oakley, Diane and Kenneally, Kelly (2015), "Retirement Security 2015: Roadmap for Policy Makers Americans' Views of the Retirement Crisis," National Institute on Retirement Security, p.1. Available at *http://www.nirsonline.org/storage/nirs/documents/2015%20Opinion%20Research/final_opinion_research_2015.pdf,* last accessed Nov. 25, 2017.

13. For information and the recent history of legislative proposals introduced in Congress, *see http://cri.georgetown.edu/login/?redirect_to=http%3A%2F%2Fcri.georgetown.edu%2Ffederal-legislative-proposals%2F* (registration required).

14. For more detailed information about state programs and legislative proposals, *see* the Georgetown Center for Retirement Initiatives Web site at *http://cri.georgetown.edu/states/* (registration required). For an example of model legislation to establish a state-facilitated auto-IRA and a review of state auto-IRA initiatives, *see* National Conference on Public Employee Retirement Systems (NCPERS), "Secure Choice 2.0: States blazing a path to retirement security for all," July 2017.

15. V.T. Legis. S. 135, No. 69, Sec. C. Reg. Sess. 2017. This law is based on the work of the Vermont Public Retirement Study Committee's Interim Study of the Feasibility of Establishing a Public Retirement Plan Required by Act 157 of the 2016 Legislative

Session, submitted on Jan. 6, 2017. As part of the Committee's report, the Georgetown University Center for Retirement Initiatives (CRI) prepared a Review of Potential Public Retirement Plan Options for Private Sector Employees/Employers in the State of Vermont outlining the retirement security challenge in the state of Vermont and laying out various plan design retirement options that states could pursue to close retirement savings gap, including a MEP option.

16. ERISA Sec. 3(32), Sec. 4(b)(1).

17. Treas. Reg. § 1.413-3(a)(2)(i); Treas. Reg. § 1.414(l)-1(b)(1).

18. Tax Code Sec. 413(c)(4).

19. Tax Code Sec. 413; Treas. Reg. § 1.413-2 and Treas. Reg. § 414(l).

20. DOL Advisory Opinion 2012-04A, May 25, 2012.

21. 80 *Fed. Reg.* 71,936, Summary. (Nov. 18, 2015).

22. 80 *Fed. Reg.* 71,938 (Nov. 18, 2015).

23. DOL rules allow cities, counties, and other state political subdivisions to sponsor MEPs. For convenience, this discussion refers to "states," although the same federal rules apply to state political subdivisions.

24. For examples of state bills that have been introduced or passed, *see* Vermont (S. 135, No. 69, Sec. C), New Jersey (A.4853), Massachusetts (H. 2973 and S. 515), Minnesota (HF 2570 and SF 2303), and Texas (HB 3601).

25. In a state-facilitated MEP, the state or its delegate would typically be the named fiduciary and have amendment, investment, and administrative authority. The state or its delegate would be expected to control plan investment options.

26. ERISA Sec. 402.

27. ERISA Sec. 403.

28. ERISA Sec. 412(a).

29. ERISA Sec. 3(21)(A).

30. DOL Reg. § 2509.75-5.

31. ERISA Sec. 404.

32. *DeBruyne v. Equitable Life Assurance Soc'y of the United States*, 920 F.2d 457, 465 (7th Cir. 1990).

33. ERISA Sec. 404(c); DOL Reg. § 2550.404c-1.

34. ERISA Sec. 404(c)(5); DOL Reg. § 2550.404c-5.

35. ERISA Sec. 105.

36. *See Amato v. Bernard*, 618 F.2d 559, 566–67, 569 (9th Cir.1980) (noting that although ERISA does not require the exhaustion of administrative remedies, the legislative history and the text of ERISA make it clear that Congress intended for such a requirement to apply).

37. Technically, a participant may contest a claim denial in state court. However, the federal Rules of Civil Procedure give the plan the right (which is almost always exercised) to remove the case to federal court.

38. *Hardt v. Reliance Standard Life Ins. Co.*, 560 U.S. 242, 245 (2010) (quoting *Ruckelshaus v. Sierra Club*, 463 U.S. 680, 694 (1983)).

39. ERISA Secs. 406–408. Similar rules are imposed by the Internal Revenue Code.

40. ERISA Secs. 406, 408.

41. ERISA Sec. 407.

42. Tax Code Sec. 414(q).

43. Tax Code Sec. 413(c)(6).

44. Tax Code Sec. 410(b).

45. Tax Code Sec. 413(c)(1) and Sec. 413(c)(3). Certain service before the employer joins the plan may be ignored.

46. Tax Code Sec. 402(g); Sec. 415(b).

47. Treas. Reg. § 1.415(a)-1(e); *see* Treas Reg. § 1.413-6(b)(1)(i).

48. Tax Code Sec. 401(a)(2).

49. Tax Code Sec. 413(c)(2).

50. Rev. Proc. 2002-21.

51. Further, IRS instructions for completing Form 5500 annual reports and Form 5300 requests for a determination on qualification suggest that the IRS would support this view.

52. Tax Code Sec. 416.

53. Tax Code Sec. 416(g).

54. Tax Code Sec. 416(c)(2).

55. Treas. Reg. § 1.416-1, G-2.

56. Tax Code Sec. 401(k); Sec. 411(a)(1).

57. Tax Code Sec. 411(a)(2)(B).

58. Tax Code Sec. 413.

59. Tax Code Sec. 411(a)(8).

60. Note that the Tax Code is silent on the application of forfeitures in a MEP. However, the only sensible rule would be that forfeitures should be applied only with respect to the employer whose employees generated the forfeiture.

61. Tax Code Sec. 401(a) (11); Tax Code Sec. 417. Plans that include annuity payment options also must allow the spouse a right to a 50 percent survivor annuity.

62. Tax Code Sec. 401(k)(2)(B).

63. To reduce costs and avoid missing participant problems, many plans automatically cash-out employees with small balances ($5,000) on leaving.

64. *See* IRS Notice 2002-4, 2002-1 C.B. 298.

65. Treas. Reg. § 1.413-2(a)(3)(iv).

66. Rev. Proc. 2016-51.

67. Rev. Proc. 2016-51; Sec. 11.03.11.

68. There have been dozens of class action suits against sponsors and vendors seeking return of too-high fees. *See e.g.*, "Uptick in Fee Litigation Reshaping 401(k) Industry," Bloomberg BNA *Pension & Benefits Daily* (6/9/16).

69. DOL letters.

70. Tax Code Sec. 414(l).

71. The Investment Company Act of 1940 (40 Act) regulates most mutual funds. Group trusts are pooled investment vehicles that limit investors to qualified plans, IRAs, and certain other tax-favored plans. Rev. Rul. 81-100, 1981-1 C.B. 326. Group trusts may register under the 40 Act.

72. *See* Samaritan Health Systems, SEC No-Action Letter (Dec. 14, 1993; Communications Workers of America, SEC No-Action Letter (Jan. 27, 1980).

73. Sec. 3(a)(2) of the 33 Act; Sec. 3(c)(11) of the 40 Act.

74. *See* 80 *Fed. Reg.* 71,938 (Nov. 18, 2015).

75. ERISA Sec. 514(e).

76. 29 CFR 2510.3-2(d); 40 *Fed. Reg.* 34526 (Aug. 15, 1975).

77. ERISA Sec. 514(a).

78. IRS (2016), "COLA Increases for Dollar Limitations on Benefits and Contributions." Available at *https://www.irs.gov/retirement-plans/cola-increases-for-dollar-limitations-on-benefits-and-contributions,* last accessed Nov. 25, 2017.

79. IRS (2016), "Traditional IRAs." Available at *https://www.irs.gov/retirement-plans/traditional-iras,* last accessed Nov. 25, 2017.

80. IRS (2016), "Retirement Topics—Required Minimum Distributions (RMDs)." Available at *https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-required-minimum-distributions-rmds,* last accessed Nov. 25, 2017.

81. IRS (2016), "Roth IRAs." Available at *https://www.irs.gov/retirement-plans/roth-iras,* last accessed Nov. 25, 2017.

82. Leakage is a term to refer to plan fund withdrawals made by participants from IRAs or 401(k) defined contribution plans. Data from HelloWallet, for example, suggests that 75 percent of 401(k) plan participants breached their savings because of basic money management problems, and 26 percent of 401(k) participants used their 401(k) savings for nonretirement needs. Fellowes, Matt and Willemin, Katy (2013), "The Retirement Breach in Defined Contribution Plans: Size, Causes, and Solutions," HelloWallet. Available at, *http://bit.ly/1pTax Code7x*, last accessed Nov. 25, 2017.

83. IRS (2016), "401(k) Resource Guide—Plan Participants—General Distribution Rules." Available at *https://www.irs.gov/retirement-plans/plan-participant-employee/401k-resource-guide-plan-participants-general-distribution-rules*, last accessed Nov. 25, 2017.

84. IRS (2015), Roth IRAs in "Publication 590-B, Distributions from Individual Retirement Arrangements (IRAs)." Available at *https://www.irs.gov/publications/p590b/ch02.html#en_US_2015_publink1000231061,* last accessed Nov. 25, 2017.

85. IRS (2016), "Traditional and Roth IRAs." Available at *https://www.irs.gov/retirement-plans/traditional-and-roth-iras,* last accessed Nov. 25, 2017.

86. S. 1383, the Retirement Security Act of 2017, allows small businesses to join MEPs without a common interest requirement. In 2016, H.R. 6396, the Retirement Security for American Workers Act of 2016, also provided for pooled employer plans without a common interest requirement.

87. In 2017, Rep. Vern Buchanan (R-FL) introduced H.R. 854, the Retirement Security for American Workers Act, which amends the Internal Revenue Code of 1986 so that multiple employer plans that meet certain criteria may not be disqualified or otherwise lose tax-favored status because one or more participating employers fail to take actions required with respect to the plan. In the previous session, S. 3471, the Retirement Enhancement and Savings Act of 2016, also included such provisions.