FRANKLIN TEMPLETON INVESTMENTS

RETIREMENT LEGISLATION & REGULATION

DOL Proposes to Facilitate Association Retirement Plans

Prepared for Franklin Templeton by Davis & Harman LLP

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Department of Labor (DOL) Proposes to Facilitate Association Retirement Plans (ARPs)

On October 22nd, the Department of Labor ("DOL") released proposed regulations that would apply a new interpretation of the definition of "employer" under the Employee Retirement Income Security Act of 1974 ("ERISA"). The purpose of the proposal is to facilitate the creation and maintenance of multiple employer retirement plans ("MEPs"), which the proposal calls "Association Retirement Plans" or "ARPs," by making it easier for employer groups and associations to maintain plans that cover unrelated employers. (One way to think about the new ARP structure is as a subset of MEPs.) The proposed rules also clarify and confirm the current ERISA treatment of retirement plans maintained by certain Professional Employer Organizations ("PEOs").

This proposal is in direct response to President Trump's August 31, 2018 Executive Order, which directed the DOL to "clarify and expand the circumstances under which United States employers, especially small and mid-sized businesses, may sponsor or adopt a MEP as a workplace retirement option for their employees, subject to appropriate safeguards." Given the speed by which DOL released the proposal, it appears that DOL was well along in drafting the proposal when the Executive Order was issued. DOL had a head start in part because this ARP proposal is very similar in terms of its conditions and constraints to a rule finalized in June 2018 that facilitated "Association Health Plans" or "AHPs."

As expected, due to statutory constraints the proposal is narrower than the MEP provisions that are included in legislation pending in Congress (discussed at the end).

Legal Context. ERISA provides that a retirement plan must be sponsored by an "employer," but it defines employer to include a person acting "indirectly in the interest of an employer" and "a group or association of employers acting for an employer in such capacity." Historically, DOL has interpreted this definition to mean that, if a group of unrelated employers wishes to participate in a retirement plan that is considered a *single* plan for ERISA purposes, then the plan must be sponsored by a "bona fide" employer group or association that has a sufficiently close economic or representational nexus to the participating employers that is unrelated to the provision of benefits. In English, this means that small employers generally must sponsor their own plan unless they can join a plan of a trade association or similar group. This limits the opportunities for small employers to enjoy the economies of scale that larger employers can achieve with their retirement plans and requires small employers to separately comply with ERISA compliance rules such as filing a Form 5500 annual report.

DOL's proposal would take a step forward – albeit a small step – to expand the circumstances under which employers could join together to participate in a single MEP. The proposal continues to require that the sponsoring entity be a bona fide group or association of employers and that the participating employers share some commonality of trade or geography, as described below. To state the obvious, DOL's goal, which is also the expressed goal of the Trump Administration, is to broaden the availability of workplace retirement plans while reducing the administrative costs of plan establishment and maintenance.

New Guidelines for Association Retirement Plans. The proposal would supersede the prior DOL advisory opinions that addressed the conditions under which a "bona fide" group or association of employers would be deemed to be acting in the interest of its employer members for purposes of satisfying the ERISA definition of "employer." Under the proposal, a group or association would be bona fide if certain criteria described below are met. The criteria track those applied in the final AHP regulations, with the exception of a health nondiscrimination rule that does not appear to be appropriate for retirement plans.

Specifically, under the proposal the group or association must:

- Have a formal organizational structure;
- Be controlled by its employer members (and the employer members that participate in the plan control the plan);
- Have at least one substantial business purpose unrelated to offering and providing employee benefits to its employer members; and
- Limit plan participation to employees and former employees of employer members, and their beneficiaries.

In addition:

- The ARP must be a defined contribution plan (e.g., a 401(k) or 403(b) plan) and may not be a defined benefit pension plan.
- Each employer participating in the ARP must act directly as an employer of at least one employee participating in the ARP.
- The group or association generally may not be a bank, trust company, insurance issuer, broker-dealer, or other similar financial services firm (including pension record keepers and third-party administrators), or owned or controlled by such a financial services firm (or its subsidiary or affiliate). This is a very important limitation in the proposal. It means that financial services firms may not, on their own, sponsor an ARP and must work with a group or association that can satisfy the criteria listed above.
- Employer members of a bona fide group or association must have a "commonality of interest." For this purpose, members of the group or association would have to be (1) in the same trade, industry, line of business, or profession; or (2) have a principal place of business within a region that does not exceed the boundaries of the same state or the same metropolitan area (even if the metropolitan area includes more than one state).

Those readers who have followed the MEP issue for some time will naturally ask what sorts of arrangements the foregoing would allow that are not allowed under the DOL's existing guidance. A good example is a plan sponsored by a state or city chamber of commerce or business league; current DOL guidance has been interpreted not to allow these organizations to sponsor a MEP.

Treatment of Working Owners. The proposed regulation, like the AHP regulation, would allow a working owner of a trade or business without common law employees to qualify as both an employer and as an employee of the trade or business. Effectively, this means that sole proprietors and other gig workers would be allowed to participate in the ARP even though the business has no common law employees. (Normally, ERISA does not apply to plans covering only a sole proprietor.) To qualify as a working owner, a person would be required to (1) work at least 20 hours per week or 80 hours per month, on average, in his or her trade or business, or (2) have wages or self-employment income from the trade or business that at least equals the owner's cost of coverage in any group health plan sponsored by the group or association in which the individual is participating or is eligible to participate.

Delegating Fiduciary Liability. In a typical MEP – and DOL contemplates this would similarly occur with its new ARP proposal – a participating employer signs a participation agreement or similar contract that lays out the rights and obligations of the MEP sponsor and the participating employer. Typically, although not required, the MEP sponsor takes on responsibility for compliance with the requirements of ERISA, including reporting, disclosure, and fiduciary obligations. But DOL's longstanding position is that the participating employer cannot relieve itself of all fiduciary responsibilities, and must prudently select and monitor the arrangement over time. The proposal would not change this longstanding framework; it would simply make it easier for employers to access a MEP.

PEO Plans. A PEO is an organization that, by contract, agrees to perform for its client employers functions typically performed by an employer, such as payroll and human resource management. The proposal would establish criteria that must be met for a PEO to qualify as a "bona fide" PEO that is capable of establishing a MEP covering the employees of client employers. Many PEOs have been offering retirement plan coverage for client employers for many years, and the DOL's proposal largely confirms the legal position PEOs have taken that these plans qualify as single ERISA plans.

Pending Legislation is Broader. The proposal differs in significant ways from leading legislative proposals pending in Congress and DOL notes that the proposal is more limited because the proposal relies solely on the DOL's authority to promulgate regulations administering ERISA. The most prominent of the legislative proposals are the Family Savings Act (H.R. 6757), which passed the House of Representatives on September 27, 2018, and the Retirement Enhancement and Savings Act (S. 2526), which is pending in the Senate and contains very similar MEP provisions to those in the Family Savings Act. In some ways, the DOL proposal goes beyond legislative proposals (e.g., in the clarification of the treatment of PEOs). In other ways, the DOL proposal is narrower, including:

- The DOL proposal provides that a bona fide group or association of employers must have at least one substantial business purpose unrelated to offering and providing retirement plan coverage or other employee benefits. Leading legislative proposals do not include this requirement.
- The DOL proposal specifically prohibits a financial institution from sponsoring a MEP. Leading legislative proposals do not include this restriction. (A financial institution may face other limitations and constraints in operating a MEP, such as avoiding ERISA's prohibited transaction rules if it selects its own investment products.)
- Unlike the leading legislative proposals, the DOL proposal includes a requirement that the participating employers must "control" the MEP.
- Unlike the leading legislative proposals, the DOL proposal requires that all employers participating in a MEP must either (1) be in the same line of business, or (2) have a principal place of business in the same region that does not exceed the boundaries of a single state or metropolitan area.

One way to summarize the differences between the leading legislative proposals and the DOL's ARP proposal is that the legislative proposals are intended to allow truly "open" MEPs that could be, potentially, offered nationwide, while the DOL's proposal is focused on expanding the types of organizations that can sponsor "closed" MEPs.

Next Steps. It is important to keep in mind that this is just a proposal on which DOL is seeking comments. The comment period ends on December 24, 2018, and we would anticipate robust comments because of the importance of this issue to stakeholders interested in retirement plan policymaking. Given that this issue is the subject of an Executive Order from President Trump, we anticipate that DOL will prioritize finalization of the regulation in 2019.

DOL's proposal does not address a related MEP problem called the "one bad apple rule," which is an Internal Revenue Code issue under which the disqualifying action of one participating employer can jeopardize the tax-qualification of the entire MEP. President Trump's August 31st Executive Order directs the Department of Treasury to examine that issue within 180 days of the date of the order.

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Franklin Templeton Distributors, Inc.

One Franklin Parkway

San Mateo, CA 94403-1906

(800) DIAL BEN® / 342-5236

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