

LAW & POLICY GROUP

GRIST

IRS PROPOSES RELIEF FROM ‘ONE BAD APPLE’ RULE FOR DC MULTIPLE-EMPLOYER PLANS

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Just-released IRS [proposed regulations](#) would make it easier for employers to participate in defined contribution (DC) multiple-employer plans (MEPs). If certain conditions are satisfied, the proposal would provide relief from the “one bad apple” rule, which says a violation of the plan qualification rules by one participating employer can jeopardize the entire MEP’s tax-qualified status. The regulations won’t take effect until finalized and cannot be relied on in the meantime. Comments on the proposal are due Oct. 1.

RELIEF FROM THE ONE-BAD-APPLE RULE

Both “open” MEPS sponsored by unrelated employers and “closed” MEPs sponsored by related employers are subject to the one-bad-apple rule (called the “unified plan rule” in the proposal). However, the rule is often perceived as a greater deterrent to open MEPs due to the lack of control among unrelated participating employers.

Highlights of relief. The proposal would allow a DC MEP to avoid disqualification for a failure by an “unresponsive participating employer” (UPE) — one that is unwilling or unable to correct the failure or unresponsive to inquiries from the MEP’s administrator about a potential failure. The relief would be available if the following conditions are satisfied:

- The MEP satisfies certain eligibility requirements, including having policies and procedures (formal or informal) in place to ensure compliance with applicable Internal Revenue Code requirements, and is not under IRS examination. The plan would also need language that addresses a participating employer’s failures. IRS intends to issue model language for this purpose once the regulations are finalized.
- The plan administrator provides a notice to the UPE about the failure and a 90-day opportunity for the UPE to correct the failure or initiate a spinoff of plan assets and account balances held on behalf of the UPE’s employees. If the UPE does not take appropriate action after receipt of the notice, a second notice would get sent within 30 days after the 90-day period expires. A third notice (with similar timing)

would go out if the UPE remains unresponsive after receipt of the second notice. Copies of this final notice would be sent to the Department of Labor (DOL) and the UPE's employees and beneficiaries.

- The plan administrator initiates a spinoff-termination if the UPE fails to take remedial action or initiate a spinoff by the last deadline (as late as 330 days after the initial notice).
- The plan administrator complies with any information request in connection with an IRS examination of the spun-off plan.

Relief unavailable if plan under examination. The relief would not be available to a MEP that is under examination or criminal investigation by IRS on the date when the first notice is provided to the UPE. For this purpose, IRS treats a MEP as being "under examination" if it has been notified of a pending examination or is aggregated for nondiscrimination testing with another plan that is under examination.

Reporting spinoffs to IRS. The MEP administrator would have to report any spinoff or spinoff-termination from a MEP to IRS (in accordance with forms, instructions and other guidance). IRS anticipates issuing a new form or revising an existing one for this purpose.

Qualification of spun-off plan. When a plan is spun off by either the UPE or the plan administrator, any qualification failure will be a failure with respect to the spun-off plan, not the MEP. If the plan administrator initiates a spin-off termination, distributions made from the spun-off plan would not lose eligibility for rollover solely because of the qualification failure.

REQUEST FOR COMMENTS

Comments are due Oct. 1. IRS requests comments on several areas of the proposal, including:

- Under what circumstances should the exception be available to defined benefit plans?
- Should a DC MEP have to meet additional requirements to be eligible for the exception?
- In a spinoff, how should the MEP treat participants with assets attributable to multiple employers?

IRS is also requesting comments on steps that DOL should take to help implement these regulations. DOL has noted that a plan administrator implementing a spinoff may be concerned about its fiduciary responsibilities and potential prohibited transactions. IRS encourages commenters to address these issues and will forward copies of those comments to DOL.

GOVERNMENT PUSH FOR OPEN MEPS

The proposal comes in response to a 2018 [executive order](#) (EO) from President Trump directing Treasury and DOL to expand access to workplace retirement plans. The EO specifically mentions expanding access to MEPS, saying these plans are "an efficient way to reduce administrative costs of retirement plan establishment and maintenance and would encourage more plan formation and broader availability of workplace retirement plans, especially among small employers."

DOL finalizing relief from common nexus rule. The EO also directs DOL to relax another significant hurdle to MEPs: the “common nexus” requirement. This rule says a MEP's participating employers must have a genuine organizational relationship unrelated to providing benefits. DOL last year [proposed](#) to relax this requirement by also allowing MEPs established by:

- A group or association of unrelated employers in the same industry or geographic location
- Professional employer organizations (PEOs) that contractually assume certain employment-related functions for their clients

The final DOL rule is currently under review by Office of Management and Budget's Office of Information and Regulatory Affairs.

Congress working on open MEPs. While DOL's rule would stop short of allowing open MEPs, legislation pending in Congress — including the House-passed Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019 ([HR 1994](#)) — would permit unrelated employers to offer DC open MEPs known as “pooled employer plans.” The bill includes relief from the one-bad-apple rule that would require excising a noncompliant participating employer from the MEP, similar to the new IRS proposal.

RELATED RESOURCES

Non-Mercer Resources

- [Proposed Regulation on MEPs and the Unified Plan Rule](#) (Federal Register, July 3, 2019)
- [HR 1994](#), Setting Every Community Up for Retirement Enhancement (SECURE) Act (Congress, May 23, 2019)
- [Proposed DOL Regulation on Association Retirement Plans and Other Multiple-Employer Plans](#) (Federal Register, Oct. 23, 2018)
- [Executive Order 13847](#): Strengthening Retirement Security in America (White House, Aug. 31, 2018)

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- [SECURE Act Stalls Amid Senate 'Holds'](#) (June 25, 2019)
- [DOL Rule To Expand Multiple-Employer DC Plans Advances Amid Legal Issues](#) (June 11, 2019)
- [House Passes SECURE Act To Bolster Retirement Plans](#) (May 24, 2019)

- [Bipartisan Retirement Reforms Pass Key House Panel](#) (April 3, 2019)
- [2019 Legislative and Regulatory Outlook for Retirement Plans](#) (Feb. 5, 2019)

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