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Benefits Guide: Basics

Cash Balance, IRAs, and Other Business Plans, Multiple Employer Qualified Plans

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Multiple Employer Qualified Plans

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(10) MULTIPLE EMPLOYER QUALIFIED PLAN BASICS

(10) The Basics —

Multiple Employer Qualified Plans: Multiple employer qualified plans (MEPs) are pension, profit-sharing, and stock bonus plans maintained by more than one unrelated employer that are not established pursuant to a collective bargaining agreement. Several other types of qualified plans often are confused with MEPs; including multiemployer plans, plans maintained by two or more employers under common control, and pre-approved plans.

Plans that are not MEPs.

• ***Multiemployer Plans vs. MEPs:*** A collectively bargained plan between more than one employer and one or more unions is considered a multiemployer plan. MEPs, however, are not collectively bargained. For more on multiemployer plans, see *Collectively Bargained Multiemployer Pension Plans*.

• ***Common Control:*** If a qualified plan that would otherwise qualify as a MEP is maintained by two or more employers and all of those employers are under common control, the employers are treated as if they were a single employer for purposes of applying the IRC qualification rules and the plan is not considered to be a MEP. [1]

• ***Master and Prototype Plans:*** Certain banks, insurance companies, investment companies, and similar entities draft master and prototype plans—plan documents satisfying the requirements of ERISA and the I.R.C.—designed to be adopted by many employers. A master or prototype plan is not considered a MEP unless the employers adopting the plan otherwise meet the requirements for a MEP. [2] Even though adopting employers use documents with the same language and might pool the assets of their respective trusts into a common trust fund or other collective investment used by a master plan, this does not cause the arrangement to be considered a MEP. The IRS is phasing out master and prototype plans. [3] For more on these plans, see *Pre-Approved Retirement Plans*.

• ***State-Sponsored MEPs:*** A state-sponsored MEP that allows an employer to join if it meets specified eligibility criteria may be considered a single ERISA plan, allowing for the filing of only a single Form 5500 for the whole arrangement. To participate in the state-sponsored MEP, employers would be required only to execute a participation agreement.

Participating employers would not have to share a common employment-based nexus or other genuine organizational relationship unrelated to the provision of benefits. Under a state-sponsored MEP, each employer that chose to participate would not be considered to have established its own ERISA plan, and the state could design its defined contribution MEP so that the participating employers could have limited fiduciary responsibilities, but the duty of prudence in selecting the arrangement and monitoring its operation would continue to apply to the participating employers.[4] State-sponsored MEPs are not affected by the DOL rule, effective Sept. 30, 2019, that makes certain bona fide employer associations or professional employer organizations eligible to sponsor defined contribution MEPs.[5]

[1] I.R.C. § 1563.

[2] 26 C.F.R. § 1.401(b)-1(d)(4).

[3] Rev. Proc. 2017-41.

[4] 29 C.F.R. § 2509.2015-02.

[5] 84 Fed. Reg. 37508 (July 31, 2019).

This chapter will address privately sponsored MEPs and then explain the rules that create a single employer due to common ownership or affiliated relationships. Employers lacking common ownership or affiliations may, starting in 2021, establish open MEPs known as Pooled Employer Plans, or PEPs, under authority of the Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act), discussed at Pooled Employer Plans.

The existence of MEP status is wholly dependent on the determination of whether participating employers are related or unrelated. In general, an employer is considered to be related if the employer is under common control as defined by the I.R.C. § 414(m), § 414(n) or § 414(o). If employers are not under common control under these provisions, I.R.C. § 413 nevertheless allows such unrelated employers to participate in a MEP provided the requirements of I.R.C. § 413 are satisfied. The DOL constrains this MEP concept found in the I.R.C. by further requiring that employers share an economic nexus and commonality of interests unrelated to the MEP to participate in the same MEP. The DOL also determined that unrelated employers, under its determination, cannot participate in a single plan. Thus, historically, MEPs that provide coverage to unrelated employers under the Treasury guidance must still be considered related employers under DOL guidance for the plan to be considered a single plan. If the unrelated employers were not considered a single employer under the DOL guidance, the combined plan was not considered a single plan and, at a minimum, a separate Form 5500 annual report needed to be filed for each participating employer.

Additional Resources: TM Portfolio 353: Employee Benefit Plans and Issues for Small Employers, Who Is Really the Employer?; Benefits Guide: *Pre-Approved Retirement Plans*; *The Minimum Funding Standard*; *Annual Reporting on Form 5500*; TPS, ¶ 5560.06.C. Multiple Employer Plans.

(20) MULTIPLE EMPLOYER QUALIFIED PLAN FEATURES

(10) Multiple Employer Qualified Plan Features: The Basics —

MEPs are explicitly recognized under I.R.C. § 413(c) which only requires that the MEP must satisfy all applicable I.R.C. requirements. To be tax-qualified, the MEP, and its related trust, must satisfy all of the I.R.C. qualification requirements that apply to plans sponsored by single employers. In fact, the employees of each employer that contributes to a MEP are generally treated as if they were employed by a single employer in applying the I.R.C. requirements relating to:

- minimum coverage and participation;
- nondiscrimination;
- exclusivity of benefits;
- vesting;
- funding; and
- limits on the deductibility of contributions.[6]

[6] I.R.C. § 413(c).

A limitation on the I.R.C. and Treasury's allowance of MEPs was the “one bad apple” rule (also referred to as the unified plan rule) which dictated that a qualification failure by one employer in the MEP would disqualify the entire MEP, due to the fact that the above enumerated qualification requirements had to be satisfied on a MEP-wide basis.

Conversely, DOL guidance concluded that participation by unrelated employers within a single qualified plan, despite being explicitly sanctioned under I.R.C. § 413(c), was not permitted. As a result, under this guidance, employers could only participate within the same qualified plan if those employers share an economic nexus and commonality of interests unrelated to the MEP.[7]

[7] DOL Op. Ltr. 2012-03A.

Practice Tip: This has historically resulted in qualified plans that are considered MEPs under I.R.C. § 413(c) as being deemed, by the DOL--because the employers within the plan share an economic nexus and commonality of interests unrelated to the MEP--either a “single” employer plan or a collection of separate unrelated plans. This regulatory mismatch created challenges with respect to compliance, administration, and reporting.

Practice Tip: The SECURE Act, though it eliminated the “one bad apple rule” for PEPs that could cause the disqualification of the entire MEP if one participating employer was disqualified, did not change the § 413(c) qualification rules nor eliminate the existing types of MEPs.

The DOL has evaluated multiple MEP structures to determine if unrelated employers participating in a MEP that otherwise satisfy applicable IRS guidance would be considered a single employer by the DOL and has repeatedly concluded that a § 401(k) plan maintained for employees of a limited-purpose corporation designed to operate the plan and for the employees of unrelated

employers is not a "single employer" plan.[8] The DOL has also found no employment-based common bond between the corporation or a registered investment adviser.[9] In addition, having unrelated employers sign identically worded documents is not enough for the DOL to conclude that the "employers have established or maintain a single plan for purposes of ERISA."[10] Similarly, a collection of separate, apparently abandoned, employee benefit plans with no employment-based common bond does not appear to qualify as a MEP for DOL purposes.[11]

[8] DOL Op. Ltr. 2012-04A.

[9] DOL Op. Ltr. 2012-04A.

[10] DOL Op. Ltr. 2012-04A.

[11] DOL Op. Ltr. 2012-03A.

Bona Fide Group or Association. MEPs consisting of employers that are a part of a bona fide group or association of employers can be considered a related employer by the DOL so as to justify a defined contribution MEP being treated as a "single employer" plan. Under DOL regulations, a group or association of employers is considered bona fide if it:

- has a formal organizational structure with a governing body and bylaws or other similar indications of formality;
- is controlled, in form and substance, by its employer members, who also must control the MEP;
- has at least one substantial business purpose unrelated to offering and providing employee benefits to its employer members, though the primary purpose of the association or group may be to offer and provide MEP coverage;
- limits plan participation to employees and former employees of employer members and their beneficiaries;
- has members with a commonality of interests, for example, the employers are either (i) in the same trade industry, line of business, or profession or (ii) have a principal place of business within a region that does not exceed the boundaries of the same state or same metropolitan area; and
- ensures that each employer acts directly as an employer for at least one employee participating in the MEP.[12]

[12] 29 C.F.R. § 2510.3-55(b)(1)(i) through 29 C.F.R. § 2510.3-55(b)(1)(vi).

On the other hand, a financial institution, such as a bank, trust company, insurance issuer, broker-dealer, or other similar financial services firm, including record-keepers and third party administrators, or an entity owned or controlled by such a financial services firm, cannot sponsor an MEP as the collection of unrelated employers would not be considered bona fide group or association of employers.[13]

[13] 29 C.F.R. § 2510.3-55(b)(1)(vii).

Bona Fide HR Company, or PEO. A bona fide human-resource company, or PEO, also can offer an MEP, treated as a "single employer" plan, rather than individual plans adopted by each client employer. To be bona fide, the PEO must:

• provide substantial employment functions and maintain adequate records related to such functions;

• have substantial control over the functions and activities of the MEP, as the plan sponsor, plan administrator, and plan named fiduciary;

• ensure that each client-employer adopting the MEP is the direct employer of at least one employee participating in the MEP; and

• be available only to employees and former employees of the PEO and its clients, and their beneficiaries. [14]

[14] 29 C.F.R. § 2510.3-55(c)(1).

Whether a PEO performs substantial employment functions on behalf of its client employers is determined based on the facts and circumstances of the particular situation. As a safe harbor, a PEO is considered to perform such functions if, for each client-employer employee that participates in the MEP:

• the PEO assumes responsibility for and pays wages to employees of those client-employers, without regard to the receipt or adequacy of payment from those client-employers;

• the PEO assumes responsibility for and reports, withholds, and pays any applicable federal employment taxes for those client-employers, without regard to the receipt or adequacy of payment from them;

• the PEO plays a definite and contractually specified role in recruiting, hiring, and firing workers of those client-employers; and

• the PEO assumes responsibility for and has substantial control over the functions and activities of any employee benefits that the service contract may require the PEO to provide, without regard to the receipt or adequacy of payment from those client employers for such benefits. [15]

[15] 29 C.F.R. § 2510.3-55(c)(2).

Coordinated Interagency Response. In response to this divergence, solutions to coordinate the position of the Department of Treasury and the DOL were sought both on a regulatory and a statutory front. *Executive Order 13847*, signed Aug. 31, 2018, directed the Treasury and DOL to study the expansion of MEPs and propose new rules to reduce the administrative burdens and costs (which disproportionally impacted smaller employers) of forming such plans. [16] This led to the introduction of proposed regulations issued by IRS in July 2019 which provided that a defined contribution MEP would not be disqualified if an employer participating in the MEP fails to satisfy a qualification requirement or provide information needed to determine compliance with a qualification requirement. [17] This was intended to address the “one bad apple” rule which causes the non-compliance of a single participating employer in a MEP to be a disqualifying defect for the entire MEP and for all employers participating therein. The

DOL, pursuant to *Executive Order 13847*, similarly issued finalized regulations that permit employers in a city, county, state, or a multi-state metropolitan area, or in a particular industry nationwide to organize themselves into an association and combine to provide a defined contribution MEP for their employees[18] and requested comments as to whether the then final regulation should be expanded even further to permit "Open MEPs"–or MEPs that allow for participation of wholly unrelated employers; not limited to a geographical area, a trade association, or a specific industry.[19]

[16] Executive Order No. 13,847, 83 Fed. Reg. 45321 (Sept. 6, 2018).

[17] Prop. 26 C.F.R. § 1.413-2(g), 84 Fed. Reg. 31777 (July 3, 2019).

[18] 29 C.F.R. § 2510.3-55.

[19] 84 Fed. Reg. 37512 (July 31, 2019).

(15) **Pooled Employer Plans** —

Effective for plan years beginning after Dec. 31, 2020, wholly unrelated employers[20] can participate within a single defined contribution MEP, or pooled employer plan (PEP) under provisions of the Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act).

[20] 29 U.S.C. § 1002(2)(C), as added by Further Consolidated Appropriations Act, 2020, Pub. L. 116-94, Div. O, § 101(b).

The SECURE Act's detailed rules are intended to reduce the administrative burdens and costs, which disproportionally impacted smaller employers, of forming retirement plans. The SECURE Act also addressed the "one bad apple" rule – statutorily – by providing that the failures of one employer within a PEP does not risk the tax qualified status of the MEP for other unrelated participating employers.[21]

[21] I.R.C. § 413(e) and 29 U.S.C. 1002(44)(C), as added by Further Consolidated Appropriations Act, 2020, Pub. L. 116-94, Div. O, § 101(a) and § 101(c), respectively.

Practice Tip: Following the SECURE Act's enactment, it is anticipated that the regulatory focus will shift from implementing the prior issued proposed regulations by the Treasury and the final regulations by the DOL, to implementing the terms of the SECURE Act and PEPs.

By permitting wholly unrelated employers to participate within a single defined contribution plan, or PEP, the SECURE Act vitiated the DOL's position that only employers with a sufficient relationship are permitted to participate within a single plan. In order to be a PEP, a MEP must:

- designate a PEP provider and provide that the PEP provider is the named fiduciary of the PEP;

- designate one or more trustees who are not employers participating within the PEP and who are responsible for collecting contributions to, and holding assets of, the PEP;

• require the trustees to implement a written contribution collection procedure which is reasonable, diligent, and systematic;

• provide that each employer retains fiduciary responsibility for:

• the selection and monitoring of the PEP provider; and

• the selection of investment and management of the portion of the PEP's assets attributable to the employees of the employer, to the extent not otherwise delegated to another fiduciary by the PEP provider and subject to the provisions of ERISA § 404(c).

• not subject employers in the PEP, and participants and beneficiaries, to unreasonable restrictions, fees, or penalties with regard to ceasing participation in the PEP, receiving distributions from the PEP, or otherwise transferring assets of the PEP;

• require the PEP provider to provide employers in the PEP any required disclosures, including but not limited to, information to enable the employer to facilitate the selection and monitoring of the PEP provider by employers in the PEP; and

• require each employer in the PEP to take all actions the PEP provider deems necessary to administer the PEP and meet any qualification requirements.[22]

[22] 29 U.S.C. 1002(43), as added by Further Consolidated Appropriations Act, 2020, Pub. L. 116-94, Div. O, § 101(c).

The PEP provider must:

• be designated by the PEP's terms as a named fiduciary, as the plan administrator and as the person responsible for performing all administrative acts, including conducting proper testing with respect to the PEP and the employees of each employer in the PEP, to ensure that the PEP meets the necessary qualification requirements and that each employer within the plan takes the necessary acts to maintain the PEP's tax qualifies status;

• register as a pooled plan provider with the Treasury Secretary;

• acknowledge that such person is a named fiduciary; and

• ensure that all parties under the PEP that handle plan assets are properly bonded in accordance with the requirements of ERISA.[23]

[23] I.R.C. § 413(e) and 29 U.S.C. 1002(44), as added by Further Consolidated Appropriations Act, 2020, Pub. L. 116-94, Div. O, § 101(a) and § 101(c), respectively.

Working owners without employees will be able to participate in a PEP, provided they meet certain regulatory criteria as reasonably determined by a responsible plan fiduciary. Working owners include anyone with an ownership right in a trade or business, including a partner or other self-employed individual, and anyone who earns wages or self-employment income from the trade or business by providing personal services to it for an average at least 20 hours per week or 80 hours per month. [24]

[24] 29 C.F.R. § 2510.3-55(d).

Form 5500 Filing: Under the SECURE Act, MEPs that satisfy the PEP rules will only be required to file one annual Form 5500. This solves an issue for plans that satisfied the rules under I.R.C. § 413(c) to be treated as a MEP for the purposes of the Treasury rules but were considered multiple unrelated plans by the DOL. Prior to the SECURE Act, PEPs had to include in their annual Form 5500 filings a list of participating employers and a good-faith estimate of the percentage of total contributions made by such employers during the plan year and must include the identifying information for the person designated as the PEP provider. [25] MEPs that were deemed a "single employer" were permitted to file a single Form 5500 (with certain caveats) but are required to include in their annual Form 5500 filings a list of participating employers and a good-faith estimate of the percentage of total contributions made by such employers during the plan year. [26] The SECURE Act clarifies that MEPs that satisfy the PEP rules must only file one annual Form 5500. PEPs must include in their annual Form 5500 filings a list of participating employers and a good-faith estimate of the percentage of total contributions made by such employers during the plan year and must include the identifying information for the person designated as the PEP provider.

[25] 29 U.S.C. § 1023, as amended by Further Consolidated Appropriations Act, 2020, Pub. L. 116-94, Div. O, § 101(d).

[26] 2018 Instructions for Form 5500-SF.

Practice Tip: Since a PEP is also considered a MEP under I.R.C. § 413(c), it is anticipated that the annual filing for the PEP will include the same information otherwise required to be filed for MEPs. Smaller PEPs may also be eligible to file a simplified annual report if the plan, as a whole, has less than 1,000 participants and no employer within the PEP has more than 100 participants. [27]

[27] 29 U.S.C. § 1023, as amended by Further Consolidated Appropriations Act, 2020, Pub. L. 116-94, Div. O, § 101(d).

(20) **Coverage and Participation Rules for MEPs** —

The employees of each of the employers that maintain a MEP must be treated as if they were employed by a single employer in applying to I.R.C.'s minimum coverage and participation rules. In other words, those rules are applied on an employer-by-employer basis notwithstanding the "deemed" single employer status.

Every qualified plan must satisfy at least one of three minimum coverage rules:

• The first, or general test, requires that a plan cover 70% of an employer's eligible employees. The following example shows how the general test applies in a MEP context.

Example: Alpha Co. and Beta Inc. are unrelated employers maintaining a multiple employer qualified plan and seek to satisfy the minimum coverage requirement that the plan cover 70 percent of all employees of an employer. In the aggregate, the plan covers 75% of all eligible employees of the two employers. However, the plan covers 65% of Alpha's eligible employees and 80% of Beta's. Since the minimum coverage rules are applied on an employer-by-employer basis, Alpha will not satisfy the 70% test, but Beta will.

• If the general test is not satisfied, the qualified plan can still satisfy coverage testing by satisfying the ratio percentage test, which requires that the plan benefit a classification of employees that does not allow more than a reasonable difference between the percentage of an employer's highly compensated employees who are covered and a similarly computed percentage for non-highly compensated employees. [28]

• If neither the general test nor the ratio percentage test is satisfied, the qualified plan can still satisfy coverage testing by satisfying the average benefits percentage test, which requires that a plan benefit (i) a nondiscriminatory classification of employees and that the (ii) average benefit percentage (benefits expressed as a percentage of compensation) for non-highly compensated employees be at least 70 percent of the average benefits percentage for highly compensated employees. [29]

[28] I.R.C. § 410(b); 26 C.F.R. § 1.410(b)-8.

[29] I.R.C. § 410(b)(2)(A).

An employer in a MEP must satisfy coverage testing based on its employees alone and, if relying on the average benefit test, must also, standing alone, benefit at least the lesser of 50 employees or 40% of employees determined as to each employer. [30]

[30] I.R.C. § 401(a)(26).

Once coverage testing is passed, discrimination testing for contributions and benefits in an MEP apply as if all of the MEP's participants were employed by a single employer. [31]

[31] I.R.C. § 413(c)(4).

Practice Tip: Unlike collectively bargained plans, whether a MEP discriminates with respect to contributions or benefits is not determined by testing separately each group of employees who are subject to the same benefit formula.

One Bad Apple for MEPs . Under Treasury's proposed rules in July 2019,[32] a qualification failure by one employer within a MEP, for example a failure to satisfy discrimination testing as to contributions, will not necessarily disqualify a MEP for all participating employers. This exception to the unified plan rule is generally available if the participating employer in a MEP is responsible for a qualification failure that the employer is unable or unwilling to correct. It would also be available if the participating employer fails to comply with the plan administrator's request for information about a qualification failure that the plan administrator reasonably believes might exist. The regulations specify what is a known or potential qualification failures for these purposes.

[32] Prop. 26 C.F.R. § 1.413-2(g), 84 Fed. Reg. 31777 (July 3, 2019).

Example (known failure): A known qualification failure is a failure to satisfy a qualification requirement for a MEP that is identified by the plan administrator and is attributable solely to an unresponsive participating employer.[33]

[33] Prop. 26 C.F.R. § 1.413-2(g)(2)(iii)(D), 84 Fed. Reg. 31777 (July 3, 2019).

Example (potential failure): A potential qualification failure is a failure to satisfy a qualification requirement as to a MEP that the plan administrator reasonably believes might exist, but is unable to determine whether the qualification requirement is satisfied solely because an unresponsive participating employer fails to provide data, documents, or any other information necessary to determine whether the MEP is in compliance with the qualification requirement as it relates to that employer.[34]

[34] Prop. 26 C.F.R. § 1.413-2(g)(2)(iii)(D), 84 Fed. Reg. 31777 (July 3, 2019).

To qualify for the exception:

- the plan administrator must have established formal or informal practices and procedures reasonably designed to promote and facilitate overall compliance with applicable I.R.C. requirements, including procedures for obtaining information from participating employers;

- the plan document must include language describing the procedures that would be followed to address participating employer failures, including the procedures that the plan administrator would follow if, after receiving notice from the administrator, an unresponsive participating employer fails to take appropriate remedial action or to initiate a spinoff from the MEP.[35]

[35] Prop. 26 C.F.R. § 1.413-2(g)(2)(iii)(D), 84 Fed. Reg. 31777 (July 3, 2019).

A MEP that is under examination by the IRS would be ineligible for the exception. A MEP would be considered “under examination” in similar circumstances as under the Employee Plans Compliance Resolution System, except a MEP would not be under examination merely because it is maintained by an employer that is under an Exempt Organizations examination, that is, an examination of a Form 990 series or other examination by the Exempt Organizations Office of the IRS Tax Exempt and Government Entities Division.[36] For more on what under examination means, see *Employee Plans Compliance Resolution System*.

[36] Prop. 26 C.F.R. § 1.413-2(g)(2)(iii)(D), 84 Fed. Reg. 31777 (July 3, 2019).

The plan administrator would have to send up to three notices to the nonqualifying employer outlining the disqualification failures, with the third notice also going to participants, beneficiaries, and the DOL. The nonqualifying employer would have to take remedial action or initiate a spinoff within 90 days of receipt of the third notice. To initiate a spinoff, the nonqualifying employer would direct the plan administrator to spin off assets and account balances held on behalf of employees of that employer to a separate single-employer plan established and maintained by that employer in a manner consistent with that plan's terms. [37]

[37] Prop. 26 C.F.R. § 1.413-2(g)(2)(iii)(D), 84 Fed. Reg. 31777 (July 3, 2019).

Effective in plan years beginning after Dec. 31, 2020, the “one-bad-apple” rule is not a hindrance to MEP formation (so long as they qualify as PEPs), under the SECURE Act. which states that a MEP that qualifies as a PEP will not cause a qualification failure for the PEP as a whole resulting from the failure of one employer to satisfy the qualification requirements. For more, see Pooled Employer Plans. The means of facilitating correction of an employer unable or unwilling to correct a qualification defect in the SECURE Act merely requires the transfer of the assets attributable to the failing employer to another standalone plan and that the failing employer take responsibility for that new plan. In addition, the DOL Secretary has broad regulatory authority to detail a means of correction.

Practice Tip: As the statutory requirement of addressing an employer that is unable or unwilling to correct a qualification defect is in line with the proposed regulation for MEPs generally, it is anticipated that the regulations issued under the SECURE Act for this purpose will track the proposed regulations issued for MEPs generally and will apply uniformly to MEPs and PEPs.

(30) **Exclusive Benefit Test for MEPs** —

A qualified plan will not be tax-qualified unless it is maintained for the exclusive benefit of the participants and their beneficiaries of the sponsoring employer. In making that determination with respect to each employer maintaining a MEP, all of the employees participating in the MEP are treated as employees of each such employer. [38]

[38] I.R.C. § 413(c)(4).

Example: Hammer Co. maintains a MEP. Contributions by Hammer Co. could be allocated to employees of other employers participating in the MEP without violating the exclusive benefit rule because all the employees participating in the MEP are deemed to be Hammer employees.

The exclusive benefit test applies the same to PEPs under the SECURE Act as it does to MEPs. [39]

[39] I.R.C. § 413(e) and 29 U.S.C. 1002(44), as added by Further Consolidated Appropriations Act, 2020, Pub. L. 116-94, Div. O, § 101(a) and § 101(c), respectively.

(40) **Eligibility and Vesting in MEPs** —

The minimum eligibility and vesting rules apply to a MEP as if all the employers maintaining the MEP constitute a single employer. For example, all the hours that an employee works for each employer maintaining the MEP are aggregated in computing that employee's number of years of service for eligibility and vesting purposes. [40]

[40] I.R.C. § 413(c)(1); 29 U.S.C. § 1060(a).

Practice Tip: MEPs are treated differently from collectively bargained plans in testing whether there has been a termination, partial termination, or complete discontinuance of employer contributions, so as to require full vesting of accrued funded benefits. In a MEP, the IRS does not examine separately each group of participants who are subject to the same benefit formula to determine if a termination, partial termination, or complete discontinuance of employer contributions has occurred. Rather, whether one of these events has occurred is determined based on the experience of all of the plan's participants in the aggregate.

For more on vesting, see *Vesting Rules*.

Under the SECURE Act, each employer in a PEP is treated as plan sponsor of the portion of the PEP attributable to employees of such employer. [41] What is unclear is whether the provisions that apply to an employer under a PEP (e.g. fiduciary selection and monitoring obligations and compliance with administrative requirements) attach for only the portion of benefits accrued within the PEP from service with that specific employer, It is also possible, in the case in which an employee works for multiple employers within the same PEP, that these provisions attach based upon the most current employer with respect to whom the employee accrued benefits under the PEP.

[41] 29 U.S.C. § 1002(44)(D).

(50) **Funding Rules and Deduction Limits for Defined Benefits MEPs** —

The minimum funding standards for defined benefit qualified plans apply to a MEP as if all of the plan's participants were employed by a single employer. If the plan develops an accumulated funding deficiency, the usual two-tiered excise tax applies and is allocated among the participating employers. Similarly, the limits on deductible employer contributions are applied as if all of the participants in a MEP were employed by a single employer. [42]

[42] I.R.C. § 413(c)(4).

Generally, a MEP must use IRS-prescribed mortality tables to determine minimum funding requirements. A MEP can apply to the IRS for permission to use substitute mortality tables in lieu of the prescribed tables in the regulations. The application must be

made by the plan administrator, and the substitute mortality tables must apply on a plan-wide basis. Plan sponsors not using plan-specific mortality tables can delay application of the new rules in certain circumstances.[43] For more on mortality tables, see *Using Mortality Tables to Calculate Funding Assumptions*.

[43] 26 C.F.R. § 1.430(h)(3)-1.

To meet its minimum funding obligation, a charity or cooperative organization must comply with I.R.C. § 433, rather than the rigorous pension funding rules created under the Pension Protection Act of 2006. The Treasury Secretary may, but has yet to, prescribe, by regulation, mortality tables to be used in determining the plan's current liability under § 433(c)(7)(C).[44]

[44] I.R.C. § 433, as added by the Cooperative and Small Employer Charity Pension Flexibility Act (CSEC Act), Pub. L. No. 113-97.

A plan sponsor of an eligible charity plan can elect for the plan to stop being treated as an eligible charity plan. If a plan sponsor chooses to do that, then starting with the first day of the plan year beginning in 2014, the plan is subject to the minimum funding requirements under I.R.C. § 430 and the benefit restrictions of I.R.C. § 436.[45]

[45] IRS Notice 2015-58.

Sponsors can make this election by giving the plan administrator and the enrolled actuary written notice. Generally, this election had to be made prior to the plan's contribution deadline for the 2014 plan year. The election also could be reflected in the plan's Form 5500 Schedule SB for 2014 and, with written notice, given to the administrator and actuary by Dec. 31, 2015. Presumably, the same deadlines and notice requirements also apply to a plan sponsor's electing to stop being treated as an eligible charity plan in the 2015 and subsequent plan years.[46]

[46] IRS Notice 2015-58.

If this election is made, the plan sponsor can also elect to use the extended amortization rules under PPA §§ 104(d)(3)(B) through (G), which were added by the Cooperative and Small Employer Charity Pension Flexibility Act of 2014 (CSEC Act). These amortization rules provide funding relief for the plan that is generally comparable to the funding relief that would have applied if

- I.R.C. § 430 had applied to the plan for all plan years beginning on or after Jan. 1, 2008;
- the plan sponsor had made a 15-year amortization election under I.R.C. § 430(c)(2)(D)(iii) for the plan years beginning in 2010 and 2011, and;
- there were no previous installment acceleration amounts described in I.R.C. § 430(c)(7).[47]

[47] IRS Notice 2015-58.

A CSEC Act plan is a defined benefit plan other than a multiemployer plan that meets one of the following conditions:

• for the plan year in question, the effective date of the PPA funding rules has been delayed for the plan prior to the enactment of the Pension Relief Act of 2010, which made changes to applicable sections of the PPA;

• for periods starting on June 25, 2010, and ending on the last day of the plan year, the plan has been maintained by more than one employer and all of those employers are I.R.C. § 501(c)(3) organizations; or

• for periods starting on June 25, 2010, and ending on the last day of the plan year, the plan was maintained by an I.R.C. § 501(c)(3) employer with employees in at least 40 states and "whose primary exempt purpose is to provide services" for children. [48]

[48] IRS Notice 2015-58.

Plans created under CSEC Act are subject to certain reporting requirements, including completing portions of the Form 5500 Schedule SB.

A plan sponsor of an eligible cooperative or charity plan that was not subject to the § 436 benefit restrictions for the 2016 plan year has until Dec. 31, 2019, to amend the plan to avoid being subject to the benefit restrictions for plan years beginning on or after Jan. 1, 2017. If the plan fits the definition of a CSEC Act plan, it continues to be excluded from those rules unless the plan sponsor elects that the plan not be treated as a CSEC Act plan. [49]

[49] IRS Notice 2017-72.

Practice Tip: The funding rules and deduction limits for a MEP defined benefit plan do not apply to PEPs as a PEP is required to be a defined contribution plan. For more, see Pooled Employer Plans.

(30) **CONTROLLED GROUPS OF CORPORATIONS**

(10) **Controlled Groups of Corporations: The Basics** —

Corporations that comprise the component members of a controlled group of corporations—a group of employers having a specified degree of common ownership—are treated as if they were a single employer in applying the I.R.C. general nondiscrimination requirements, as well as the requirements relating to:

- top-heavy plans;
- funding;
- the deductibility of employer contributions;
- participation and coverage;
- vesting;
- benefit accrual;
- the maximum benefit an employee can earn under a defined benefit plan; and
- the maximum annual contribution that can be made to an employee's account under a defined contribution plan.[50]

[50] I.R.C. § 1563.

(20) **What Is a Controlled Group of Corporations?** —

A controlled group of corporations can take the form of a parent-subsidiary group (in which one corporation, known as the parent, owns a stock interest in one or more other corporations, known as subsidiaries).[51] It can also take the form of a brother-sister group (consisting of two or more corporations that are owned by the same person or groups of persons.[52] A controlled group also can consist of a combination of the above two types of groups, in which case it is called a combined controlled group.[53]

[51] I.R.C. § 1563(a)(1).
[52] I.R.C. § 1563(a)(2).
[53] I.R.C. § 1563(a)(3).

A parent-subsidiary controlled group consists of one or more groups of corporations connected through stock ownership if:

- stock representing at least 80% of the value or 80% of the total combined voting power of each member corporation (except for the stock of the common parent corporation) is owned by one or more of the group's members; and
- the common parent corporation owns stock representing at least 80% of the value or 80% of the combined voting power of at least one of the group's corporations.[54]

[54] I.R.C. § 1563(a)(3).

Example: ABC partnership owns stock possessing 80% of the total combined voting power of all classes of stock entitled to voting of S corporation. ABC partnership is the common parent of a parent-subsidiary group of trades or businesses under common control consisting of the ABC partnership and S Corporation.[55]

[55] 26 C.F.R. § 1.414(c)-2(e) Example (1)(a).

A brother-sister controlled group consists of two or more corporations in which five or fewer persons who are individuals, estates, or trusts:

- own stock representing at least 80% of the value or at least 80% of the combined voting power of each corporation in the group, and
- own stock representing at least 50% of the value or at least 50% of the combined voting power of all classes of stock of each corporation in the group.[56]

[56] I.R.C. § 1563(a)(2).

Example (brother-sister groups of trades or businesses under common control): Unrelated individuals A, B, C, D, E, and F own an interest in sole proprietorship A, a capital interest in the GHI Partnership, and stock of corporations M, W, X, Y, and Z (each of which has only one class of stock outstanding) in various proportions. Under these facts, the following four brother-sister groups of trades or businesses under common control exist: GHI, X and Z; X, Y and Z; W and Y; A and M.[57]

[57] 26 C.F.R. § 1.414(c)-2(e) Example 4.

Similar aggregation rules apply to the plans of unincorporated business entities, such as sole proprietorships and partnerships, that have common ownership.

Just as an employee who participates in more than one qualified plan sponsored by a single employer must aggregate all of such plans in determining whether he or she has exceeded the I.R.C. maximum allowable contribution or benefit, an individual employed by more than one employer with a qualified plan must aggregate all of the employers' plans in which he or she participates if the employers are under common control or are members of an affiliated service group. For more on aggregation, see *Coverage Requirements*.

(40) **AFFILIATED SERVICE GROUP RULES**

(10) **Affiliated Service Group Rules: The Basics** —

The affiliated service group rules were designed to prevent service-providing employers from setting up multiple business entities to evade or circumvent one or more of the nondiscrimination and related requirements governing qualified plans.[58]

[58] I.R.C. § 414(m).

Example: To evade a nondiscrimination rule, a medical practice places all of the doctors in one business entity and all of the support staff in a second, with the second business providing its services exclusively, or almost exclusively, to the first. A qualified plan providing a high level of benefits could then be put in place for the highly compensated doctors in the first entity while one providing lesser benefits or no plan at all could be put in place for the benefit of the non-highly compensated support staff in the second entity.

The affiliated service group rules apply various I.R.C. qualification provisions to the group in the aggregate. As with controlled groups of corporations, certain qualified plan rules are applied so that all employees of all members of the group are treated as if they were employed by a single employer. These rules include the I.R.C. general nondiscrimination rules, as well as the requirements relating to:

- top-heavy plans;
- funding;
- the deductibility of employer contributions;
- participation and coverage;
- vesting;
- benefit accrual;
- the maximum benefit an employee can earn under a defined benefit plan; and
- the maximum annual contribution that can be made to an employee's account under a defined contribution plan.[59]

[59] I.R.C. § 414(b).

For more on controlled groups of corporations, see *Controlled Groups of Corporations*.

(20) **Definitions Regarding Affiliated Service Group Rules** —

A service organization is an employer whose principal business consists of providing services in specified fields. A service organization's income consists primarily of fees, commissions, and other compensation for personal services performed by individuals.[60]

[60] I.R.C. § 414(m)(3).

Organizations in the following fields generally are considered to be service organizations:

- accounting;
- actuarial science;
- architecture;
- consulting;
- engineering;
- health;
- insurance;
- law; and
- the performing arts.

An affiliated service group consists of a service organization (an employer whose principal business consists of the performing of services) and one or more related employers. The service organization is called the first service organization (or FSO). As explained below, the related employers can be either A organizations or B organizations.[61]

[61] I.R.C. § 414(m)(2).

A first-service organization can be a partnership or a professional service corporation, but no other type of corporation. A professional service corporation is a corporation organized under state law for providing professional services that has at least one shareholder who is licensed or otherwise legally authorized to render the type of services the corporation is designed to provide.

Under proposed Treasury Department regulations, only the following professionals can form professional service corporations:

- accountants;
- actuaries;
- attorneys;
- chiropodists;
- chiropractors;
- medical doctors;
- dentists;
- professional engineers;
- optometrists;
- osteopaths;
- podiatrists;
- psychologists; and
- veterinarians.[62]

[62] Prop. *26 C.F.R. § 1.414(m)-1(c)*, 48 Fed. Reg. 8294 (Feb. 28, 1983).

An "A" organization is a service organization that:

- is a partner or shareholder in the FSO; and
- regularly performs services for the FSO or operates regularly in association with the FSO in performing services for third parties.[63]

[63] Prop. *26 C.F.R. § 1.414(m)-1(c)*, 48 Fed. Reg. 8294 (Feb. 28, 1983).

Example: Dr. Jones operates a medical practice through her professional corporation, which she owns by herself. In addition, her professional corporation owns 60% of a second corporation, which operates a medical laboratory and performs the majority of its services for the professional corporation. The corporation consisting of her medical practice is an FSO. The corporation operating the laboratory is an "A" organization. The two corporations constitute an affiliated service group.

A "B" organization is any organization, though not necessarily a service organization, for which:

• 10% or more of the interests in the organization are held by highly compensated employees of the FSO or An organization; and

• a "significant portion" of its business is performing services for the FSO or for an A organization, if those services are of a type "historically performed" by employees of the FSO or the A organization, as opposed to being performed by independent contractors. [64]

[64] Prop. *26 C.F.R. § 1.414(m)-2(c)*, 48 Fed. Reg. 8294 (Feb. 28, 1983).

Whether a "significant portion" of the business of a B organization is for an FSO or an A organization is generally a factual question. Under proposed Treasury Department regulations, a portion is deemed significant if the "total receipts percentage" is 10% or more. [65] However, if less than 5% of the organization's gross receipts are from the performance of services for the FSO or A organization, this is not considered a significant portion. [66]

[65] Prop. *26 C.F.R. § 1.414(m)-2(c)(3)*, 48 Fed. Reg. 8294 (Feb. 28, 1983).

[66] Prop. *26 C.F.R. § 1.414(m)-2(c)(2)(i)*; Prop. *26 C.F.R. § 1.414(m)-2(c)(2)(ii)*, 48 Fed. Reg. 8294 (Feb. 28, 1983).

Whether certain services were "historically performed" is based on whether such services were typical for employees in that service field on Dec. 13, 1980. [67]

[67] Prop. *26 C.F.R. § 1.414(m)-2(c)(3)*, 48 Fed. Reg. 8294 (Feb. 28, 1983).

Example (medical partnership): A medical partnership has 11 doctor-partners who own equal interests in the partnership. All 11 are highly compensated employees. Each doctor owns 1 percent of the stock in a corporation that provides medical billing services. A significant portion of these billing services are provided for the medical partnership. Billing services have historically been performed by employees of the partnership. The partnership is an FSO; the billing corporation is a B organization. The corporation and the partnership constitute an affiliated service group.

(50) SPECIAL AGGREGATION RULES FOR KEOGH PLANS

(10) Special Aggregation Rules for Keogh Plans: The Basics —

In addition to the rules requiring that employers under common control and members of an affiliated service group be aggregated for purposes of applying certain of the rules governing qualified plans, special aggregation rules apply to plans that cover one or more “owner-employees” who control the trade or business that sponsors a plan. Such plans are called “H.R. 10” or “Keogh plans.”

An owner-employee is either:

- a sole proprietor, who controls the business because he or she is a 100% owner; or

- someone who is a 10% or more owner of the capital interest or profits interest in a trade or business that is a partnership. Such owner-employees are considered to control the business if they collectively own more than 50% of the capital interest or profits interest.[68]

[68] I.R.C. § 401(c)(3).

Any plan maintained by another unincorporated business so controlled by the same owner-employee or owner-employees must be aggregated in applying the I.R.C. qualification requirements.[69]

[69] I.R.C. § 414(m).

Employees of such unincorporated trades or businesses must be included in a qualified plan that provides contributions or benefits to its employees that are not less favorable than those provided under the plan of the owner-employee.[70]

[70] I.R.C. § 414(m); TPS ¶ 5520.12.B Affiliated Service Group Rules.

Example: Roger runs a sole proprietorship and has established a profit-sharing plan covering himself as owner-employee and Sally, the firm's one common-law employee. Roger is a 60% partner in another business that has four common-law employees. That partnership must establish a qualified plan covering its employees in order for Roger to have contributions made on his behalf by the plan of his sole proprietorship. Further, if the sole proprietorship's profit-sharing plan makes contributions annually on behalf of Roger and Sally equal to 10% of their compensation, the plan will not qualify unless the plan of the partnership provides equal or greater allocations to the four common-law employees (or a comparable benefit under a defined benefit plan).

For more on Keogh plans, see TM Portfolio 353.III.A.7: Employee Benefit Plans and Issues for Small Employers, Plan Design Operations and Considerations, Special Issues for Small Employers.