Financial Services Organizations are Poised to Benefit from Legislative Movement in Multiple Employer Plans (MEPs)

Published by BridgePoint Group, LLC

As of 2016, 33% of Americans had yet to put aside any funds for retirement, with an additional 23% reporting savings of less than $10,000.[i] Historically, employer-sponsored retirement plans have played a significant role in helping Americans save for retirement; however, there remains a disparity between the solutions larger organizations are willing to provide and those available to small businesses. As a result, many elect to not offer formal programs due to their cost, complexity and associated fiduciary risk.

While recent state-mandated IRA efforts offered one potential solution to address the 28.8 million underserved small business employees, the approach has recently lost momentum under the current administration.[ii]

As awareness of the retirement savings coverage gap continues to grow, efforts in Washington are now focused on providing a privatized solution through the expansion of multiple employer plans (MEPs). While still early, the proposed legislation under the Retirement Enhancement and Savings Act (RESA) currently holds full bipartisan support and will be proceeding through the legislative process this year. BridgePoint's goal is to keep our clients informed of emerging activities and educate firms on the potential impact. It is our perspective that if passed, MEPs can provide both an alternative for uncovered Americans as well as a host of new opportunities for providers of retirement services.

The Benefits and Challenges of Extending Workplace Retirement Plans

According to AARP, people are 15 times more likely to build retirement savings if they are provided access to a payroll deduction savings plan at work.[iii] Social Security, while an important component of retirement, represents only about 34% of income for retired individuals.[iv] Having access to a savings plan at work is a key determinant for retirement confidence, providing a rich opportunity for our industry.

> *The limited adoption and changing political landscape of state-mandated IRAs continues to leave millions of workers without auto-enrollment plans, thus opening the door for expanded private solutions such as multiple employer plans.*

Closing the retirement savings gap is a formidable task, but it is one that as an industry we must accomplish. The adoption of programs such as MEPs to achieve this goal is only the beginning of something more disruptive to our industry. That disruption comes from the requirement to establish a significantly lower cost profile than for traditional retirement savings plans to profitably extend similar benefits in a low-balance environment.

The Evolution of Multiple Employer Plans

MEPs, defined as plans utilized by two or more employers, have been successfully deployed for years by trade associations and professional employee organizations. While enabling economies of scale, their subscription is limited due to current tax laws, ERISA rules and fiduciary liability concerns.

Washington is proposing key changes through the Retirement Enhancement and Savings Act (RESA), which unanimously passed the Senate Finance Committee in September 2016, and the Retirement Security for American Workers Act, introduced in the House in February 2017. These changes would eliminate the commonality of interest requirement, allowing multiple employer plans to reach a broader audience by reducing fiduciary risks to the employer and simplifying administration. The current laws that surround MEPs have limited widespread adoption to date, but the passage of RESA and the Retirement Security for American Workers Act would eliminate existing obstacles.

The primary difference between state-run auto IRA programs and MEPs is that the latter are truly retirement plans (rather than individual accounts) that could offer multiple investment options – giving participants the flexibility to invest their retirement portfolio in accordance with their own time horizon and risk tolerance. They would also offer employer contributions and higher contribution limits. In addition, the RESA proposal provides for a tax credit to employers who provide auto-enrollment features, and adoption is voluntary (rather than mandatory under state-sponsored programs), factors that most small businesses would find advantageous.

A Potential Area for Growth

Today, MEPs represent less than 1% of private-sector Defined Contribution plans and roughly 6% of all DC assets.[v] The alignment of industry and political forces could create a significant growth opportunity for Plan Sponsors, Providers and Advisors.

Plan Sponsors: The Department of Labor (DOL) Fiduciary Rule raised the public consciousness of the Plan Sponsor's fiduciary responsibilities. MEPs help shift many of the risks of plan sponsorship and administration to other parties, making them more attractive to Plan Sponsors.

Providers: Many financial services providers positively view MEPs as helping to address the retirement coverage gap, and potentially:

- Attracting new assets into the retirement system and their proprietary investment products
- Complementing other businesses (e.g., pension, 529, ABLE)
- Leveraging existing infrastructure to add scale
- Enhancing growth strategies for retail crossover business

- Disrupting their own business due to optimizing a low-cost model

Advisors: BridgePoint predicts that Advisors will also benefit from open MEPs. Given Advisor fee pressures, MEPs will allow scale of their business in a meaningful way within the small business market.

Specialist Advisors will look for other ways to help differentiate their practice, particularly with the introduction of all the new fiduciary services that are being offered in the market.

While retirement providers may have already adopted an opinion on such programs, what cannot be ignored is the explosion of activity that is expected ahead.

What Would Change if RESA Passes?

Currently, MEP sponsorship is limited primarily to trade associations whose members share a commonality of interest and Professional Employee Organizations (PEOs) that share a co-employer relationship with their clients. In contrast, if a plan is sponsored by a group of employers that do not share a significant commonality of interest other than participating in the same plan, the DOL's longstanding view is that they would be considered separate plans for ERISA purposes, including Form 5500 reporting. If RESA passes, any new MEPs, or Pooled Employer Plans (PEPs) as they are referred to in the bill, would adopt the new PEP structure. The commonality of interest requirement would be eliminated. (Existing MEPs would not need to meet the new requirements.)

Similarly, IRS rules impose on MEPs the "one bad apple" rule, which provides that a tax qualification error by any participating employer potentially disqualifies the entire plan. This can be particularly problematic if one employer is noncompliant with the plan's rules or simply unresponsive. The "one bad apple" rule thus imposes fiduciary risks on all participating employers. The proposed PEP plan eliminates that risk.

And finally, today, most employers technically serve as the plan's named fiduciary, but often outsource investment and other fiduciary services. If RESA passes, PEPs will be required to have a Pooled Plan Provider (PPP) as the named fiduciary to the plan. The PPP would be responsible for the administrative services, such as performing non-discrimination testing, to ensure the plan's compliance with ERISA and the tax code. The PPP could also delegate other fiduciary functions like investment selection to third parties or other named fiduciaries.

Why Would a Plan Sponsor Adopt a MEP/PEP?

The proposed PEP plan structure yields many advantages over a single employer plan.

> *Pooled employer plans will require an Administrator for all the plans, and most will also hire an Investment Fiduciary. This will significantly reduce the participating employers' fiduciary and administrative responsibilities.*

The following Plan Sponsor roles held today with single employer plans would be transferred to the Provider under proposed PEP structure:

- Monitoring of funds and conducting investment committee meetings
- Administration of participant loans
- Administration of hardship withdrawals
- Submission of year-end census data
- Administration of distribution and rollover requests for terminated employees
- Reviews and compliance testing
- Plan documents, SPD, fee and other notices

- Plan audits and 5500 reporting

Other Considerations for Providers

Retirement services Providers will be better able to scale their business under the proposed PEP plans. Under the new plan structure, there will be more consistency in the adoption of plan features. While prototype and other off-the-shelf plan designs are currently available, a PEP would allow Providers to offer a more standardized approach to allow for scale and efficiencies, thereby reducing cost and improving margins. PEPs will be easier to implement than individual plans, with the ability to meet breakeven periods on an accelerated basis. With that said, there are potential downsides. One important factor of administering the PEP is that the provider must track participation and vesting among employers. That is, if an employee moves from one participating employer to another, the employee's prior service must count towards his aggregate vesting and participation accounting. Another potential administrative concern is that while small plans do not require audits, the aggregate number employees within a PEP could invoke the audit requirement.

Providers also could further benefit as they are able to meet growth objectives and begin to differentiate their business and attract retirement specialist Advisors. Profitability could also improve as Providers will be dealing with similar plan features and underlying investment options. There may also be distribution advantages – the PEP might be marketed to a group of employers that cannot pool together currently, like those who are members of a local chamber of commerce. In other words, the PEP may be able to tap into an existing network of employers at a lower cost than winning business from small employers one at a time.

Whoever develops effective solutions for these programs will immediately become a formidable competitor in the small end of the private marketplace, and will have cemented a cost leadership position in the industry.

Advantages for Retirement Advisors

Likewise, Retirement Advisors will benefit from scale, growth and differentiation. Advisors will be allowed to better scale their businesses as they leverage 3(38) and 3(21) services across multiple plans. Growth can be achieved through cross-sell of wealth services to small business owners and their employees, and owners of the PEPs will want to grow their program and will refer warm leads to the Advisor.

Retirement Advisors will be able to stand out from their competitors and differentiate their practice by solving Plan Sponsor problems better than other Advisors. Final legislation could also allow an Advisor to establish a PEP and merge existing clients into it. This solution could become proprietary to the Advisor.

Additionally, PEPs, with their outsourced fiduciary, will be attractive to Retirement Advisors. Because

PEPs allow for scale and efficiencies due to plan structure, Advisors will be able to work with small business owners and their employees more effectively and with higher margins.

What Does This Mean for the Industry?

Will PEPs be the solution for closing the retirement coverage gap? Can this approach further prompt solutions of scale within a mature industry? While MEPs/PEPs are being debated in Washington, they also merit greater examination among financial services firms looking to incorporate market dynamics into future business strategies.

For more information on how BridgePoint can support your organization, please contact:

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[i] Kirkham, Elyssa. GoBankingRates, “1 in 3 Americans Has Saved $0 for Retirement,” March 14, 2016.

[ii] Kirkham, Elyssa. GoBankingRates, “1 in 3 Americans Has Saved $0 for Retirement,” March 14, 2016.

[iii] Harvey, Catherine, Public Policy Institute, AARP, “Access to Workplace Retirement Plans by Race and Ethnicity,” 2017.

[iv] Social Security Administration Fact Sheet, 2017.

[v] “Private Sector Pensions: Federal Agencies Should Collect Data and Coordinate Oversight of Multiple Employer Plans,” Government Accountability Office, September 2012.