*A COMPARISON OF MEWAs AND OPEN MEPs*
*SUGGESTS THAT MEPS SHOULD NOT BE REGULATED LIKE MEWAs*

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*Purpose: Open-MEPs are an important development for smaller and mid-size employers who do not have the resources or expertise to adopt their own single employer 401(k) plans and who through them can realize cost savings. Nonetheless, the United States Department of Labor ("DOL") remains skeptical about the arrangements, based mostly on its experience MEWAs, and even though MEPs can help achieve important public policy objectives under ERISA. This paper explains why DOL's experience with MEWAs should not control its consideration of open-MEPs.*

## I. A Brief History of DOL MEWA Enforcement

MEWAs[1] are designed to give employers, particularly smaller ones, access to lower cost health coverage. Many states have encouraged MEWAs and their laws for these entities often are much less stringent than they are for traditional insurers and federal regulation of MEWAs is weak. This left employees unprotected when insolvency occurred, and potentially subject to the claims of health care providers for the services provided to them.[2] Between 1988 and 1991, fraud and underfunding left plan participants with more than $123 million in unpaid claims. [3]

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[1] A MEWA is generally defined as an "employee welfare benefit plan, or any other arrangement (other than an employee welfare benefit plan), which is established or maintained for the purpose of offering or providing any [medical or welfare benefits] to the employees of two or more employers (including one or more self-employed individuals); ERISA§3(40)(A).

[2] MEWAs are generally excluded from state guaranty funds that could pay these claims. In some states, receivership laws have not allowed state insurance departments to take over insolvent MEWAs. Without receivership a MEWA can go into bankruptcy with provider and employee claims standing behind the claims of other creditors

[3] Mila Kofman et al., *MEWAs: The Threat of Plan Insolvencies and Other Challenges*, The Commonwealth Fund Mar. 2004); U.S. General Accounting Office, Employee Benefits: States Need Labor's Help Resulting Multiple Employer Arrangements, GAO/HRD – 92-40 (1962), at 2.

MEWAs first became an enforcement concern of the DOL in the early 1980s when states first began to receive complaints about unpaid claims. DOL describes the problem thusly:

> [MEWAs] are sometimes marketed using attractive but actuarially unsound premium structures that generate large administrative fees for their promoters. These high fees are often paid before any claims are paid, leaving insufficient funds available to pay for the benefits promised by the promoters.[4]

DOL's role in the regulation of MEWAs was complicated by the allocation of regulatory responsibilities to both the state and the federal levels under ERISA. Until the passage of Patient Protection and Affordable Care Act ("PPACA") substantive regulation of these arrangements was left to the states and DOL jurisdictional authority over them was limited. [5] These jurisdictional arrangements gave unscrupulous and incompetent operators an opportunity to slip between the cracks, avoiding both meaningful state and federal regulation.[6]

So, DOL did the best it could. It approached the problem by trying to discourage the formation of the arrangements in the first place by limiting the groups or associations of employers that could be considered employers.[7] In the absence of a relational link between employers in a group or association of employers other than the provision of benefits, member employers would be treated as having established their own individual welfare benefit plans. [8] The consolidated arrangement would not be a MEWA because it was not sponsored or maintained by an employer.

DOL's position has found support in the courts where one court found that a trust is not a MEWA because it recruited heterogeneous, unrelated employers[9] and by other courts where individual employers participating in "MEWAs" were found to have adopted individual single employer plans. [10]

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[4] DOL MEWA Guide.

[5] *See* ERISA §§514(b)(2)(A) and 514(b)(2)(B).

[6] According to the DOL MEWA Guide, "promoters have established and operated MEWAs, also described as 'multiple employer trusts' or 'METS', as vehicles for marketing health and welfare benefits to employers and their employees," representing that the arrangements are exempt from state insurance laws.

[7] Section 3(5) of ERISA provides that an employer includes a group or association of employers acting on behalf of employer-members to provide benefits for their employees.[7]

[8] DOL Opinion Letter No. 79-41A (June 29, 1979).

[9] *Moideen v. Gillespie*, 55 F.3d. 1478, 19 EBC 1708 (9th Cir. 1995)

[10] *See Fossen v. Blue Cross and Blue Shield of Montana, Inc.*, 660 F3d 1102 (9th Cir. 20110; *Arndt v. Concert Health Plan Ins. Co*., No. 8.09-CV-1239-T-27TBM, 48 EBC 2699 (M.D. Fla. Jan. 18, 2010)

## II. DOL Position on Open-MEPs.

DOL's applies the same legal analysis to open-MEPs that it applies to MEWAs. This analysis is expressed in two advisory opinions issued last year. [11] Its underlying concerns about MEPs restate its concerns about MEWAs. In testimony early last year before the Special Committee on Aging, United States Senate, Phyllis C. Borzi, Assistant Secretary of Labor, Employee Benefits Security Administration stated:

> The Department has more recently become aware of promoters marketing multiple employer plans, or "MEPs," that do not involve collective bargaining with an employee representative. These arrangements, often called "open MEPs," purport to allow totally unrelated businesses to join together to offer a collective pension plan. Promoters claim that these arrangements relieve businesses of their ERISA reporting and fiduciary obligations in connection with administering the plan or monitoring the plan investments and service providers. Proponents say such arrangements can provide the participating employers with a way to pool resources and reduce administrative costs.[12]

The Assistant Secretary goes on:

> The idea of "open MEPs," however, is not an established concept in ERISA. Indeed, EBSA has had difficult experiences with similar "open" employee benefit structures in the group health area. These arrangements, called "MEWAs," or multiple employer welfare arrangements, can be provided through legitimate organizations, but they sometimes are marketed using attractive, but unsound, organizational structures and generate large, often hidden, administrative fees for the promoters. In addition, certain promoters try to use ERISA's general preemption of state laws as a way to avoid state insurance or other regulation. That fact, together with the claimed separation of the employer from accountability for the plan's administration, too often put workers at risk of not getting the benefits they were promised. Bringing this type of product to the pension marketplace presents a number of complicated and significant legal and policy issues.[13]

It is clear then that DOL's current views are based primarily, if not entirely, on its old concerns with MEWAs and not on any particular evidence that open-MEPs have been subject to particular and identified abuses. The critical distinctions between MEWAs and MEPs are set forth in the grid in Part III, directly below.

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[11] DOL Opinion No. 2012-04A (May 25, 2012); DOL Opinion No. 2012-03A (May 25, 2012).
[12] Testimony given on March 7, 2012.
[13] Id.

## III. Open-MEP/MEWA Comparison Grid

| Characteristics | Open MEP | MEWA[14] |
|---|---|---|
| **Type of Plan** | Pension --- typically a 401(k) Profit Sharing Plan | Welfare --- |
| **Purpose** | Intended to give employers access to low cost deferred compensation arrangements and to reduce employers' administrative burdens. | Intended to give employers access to low cost heath coverage |
| **Subject to ERISA** | Yes. Subject to general fiduciary rules providing for protection of plan assets and participant interests. | Both ERISA and state law regulation apply. Prior to PPACA ERISA rules inadequate to protecting plan assets and participant interests. |
| **State Law Regulation** | No – Pre-emption Applies. | Yes. Absence of regulatory oversight over arrangements that were not considered subject to state insurance laws has been seen as leading to lack of accountability, fraud and mismanagement. |
| **Funding Arrangements** | Assets typically held by institutional custodians in trust. Individuals serving as trustees have been common. Investments typically managed by institutional managers or mutual funds. Permissible trustee could be limited to institutional trustee to discourage abuse. | Self-funded and held in trust or fully insured. Individuals serving as trustees have been common. |
| **History of Abuse** | Little documented.[15] | Extensively documented. |

[14] Does not consider changes made by PPACA.

[15] There is one notable case in Idaho involving a MEP administrator. United States Department of Labor, (2012) US Department of Labor alleges Idaho plan administrator misused funds. Matthew D. Hutcheson allegedly took $3.2 million from retirement plans [EBSA News Release] Retrieved from http://dol.gov/opa/media/press/ebsa/EBSA20120986.htm#.UPWBvKUZeJU. But the alleged abuse, use of plan assets by the sponsor, could as easily occur in a non-MEP situation, and could be controlled in a MEP by limiting trustees to financial institutions.

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|---|---|---|
| **Typical Risks Attendant to Arrangement** | Investment risk inherent in plan investments may result in losses to participant account balances; excessive fees; failure to pass cost savings of arrangement through to participating plans. | Lack of actuarially sound premium setting standards resulting in inability to pay claims made by employees against the fund; high fees; fraud and embezzlement. |
| **Third Party Checks on Abusive Use of Plan Assets** | Typically institutional trustees and custodians holding plan assets are accountable for plan assets; third party record keepers. Assets generally invested in regulated mutual funds. MEPs may utilize independent investment fiduciary. | Institutional and individual trustees with less accountability; assets mostly held in cash and not for investment. |

## IV. Labor Department Position Thwarts ERISA and DOL Regulatory Objectives

A. Open-MEPS can serve important objectives for small and mid-size employers. Reduction of expenses so as to enhance account balances at retirement has been explicitly and implicitly recognized in the regulations issued by DOL in the past year governing service provider and participant-level fee and expense disclosures as valuable.[16] Economies of scale can be achieved in MEPs that are not possible in most single employer plans. Investment and other expenses may be reduced with the aggregation of assets. Smaller employers may lose the benefits of these economies if MEPs are not treated as single plans.

B. Open-MEPs cannot be equated to pre-PPACA MEWAs. MEWAs were not regulated in substantive fashion under either Federal or state law. Open-MEPs are regulated strictly under the provisions of ERISA and subject to its reporting and disclosure requirements, general fiduciary obligations and prohibited transaction rules. The fiduciary requirements require employers considering a MEP to act as a prudent fiduciary and to consider the reasonableness of the arrangement and costs.

C. MEPs shift fiduciary responsibility for the administrative burdens away from relatively unsophisticated employers to professionals who are familiar with the operation and the administration of benefit plans. This

[16] *See,* for example, the regulations promulgated under ERISA §§408(b)(2) and 404(a)(5).

serves the statutory mandate of operating plans for the benefit of participants and beneficiaries by providing professional and cost effective administration of these benefits. It also encourages small unsophisticated employers to adopt plans without fear of risking liability for day to day operation of the plan that they are unprepared or unwilling to assume while retaining to the unsophisticated employer the responsibility to conduct a regular broad overview of the MEPs handling of the plan.

D. A MEP that is treated as a single plan likely will be subject to the independent qualified plan audit requirement, as many of these arrangements reach the 100 participant threshold for application of the audit requirement. Small and medium size employers participating in a MEP will lose the protection of this valuable requirement if they are treated by DOL as having established separate, single employer plans.

E. It has not been demonstrated that open-MEPs are more susceptible to abuse than non-MEP plans. A cursory review of DOL press releases describing departmental litigation in the last few years shows the great majority of actions brought by the Department have involved single employer plans, not MEPs.

## V. Recommendations

In the absence of a record of particularly identified abuses, the differences in the risks associated with MEWAs and MEPs, and in view of the significant advantages of MEPs to smaller employers, and the important Departmental regulatory objectives that can be achieved when MEPs are viewed as single employer plans, DOL should consider the following:

A. Adopting guidance that permits MEPs to exist as single employer plans, recognizing the important distinctions between MEWAs and open-MEPs and allowing MEPs to achieve important public policy objectives.

B. Establishing reasonable rules governing the operation and conduct of open-MEPs, after fact-finding, that protect plan participants, but which do not add discouraging costs, burdens, and complexities to these arrangements.

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