American Academy of Actuaries

Issue Brief

Pooled Employer Plans—Employer Considerations

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Key Points

- The Pooled Employer Plan (PEP) is a significant development that has the potential to reduce costs, complexity, fiduciary liability/risks, and administrative burdens for employers seeking to offer 401(k) retirement plans, and to simplify the process for smaller employers that do not currently offer such plans.
- There are many important issues employers consider in determining whether to offer a PEP to its employees and in selecting a Pooled Plan Provider (PPP).
- Analyzing these issues may be complex and challenging, especially for small employers, and not all of these issues are equally important to every employer.

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2021 could be a year of significant developments in private-sector retirement plans. Federal legislation enacted in December 2019, the Setting Every Community Up for Retirement Enhancement (SECURE) Act, enables new types of retirement plans that may make it easier for smaller employers to offer such plans in the future. Today, nearly 50% of workers do not have access to participate in an employer-sponsored retirement plan; the majority of these workers are employed by smaller employers.[1] Smaller employers often do not sponsor plans for a variety of reasons, including the cost to maintain a plan, potential legal liability, and the compliance and administrative efforts required.

Background

Nearly a decade ago, in an effort to expand retirement plan coverage for their citizens, some states and larger municipalities started establishing simplified retirement savings programs that could be used by employers that do not otherwise sponsor plans.[2] Although the specifics of the programs differ by jurisdiction, they essentially allow or mandate employers to offer their employees a simplified way to contribute to Individual Retirement Accounts (IRAs) overseen by the state or municipality. Such programs provide employers protections from legal liability, and reduce administrative burdens and costs (in some cases, because the sponsoring entity takes on these responsibilities and absorbs some of these costs). However, these

1 According to the Department of Labor, in 2020 only 53% of private-industry workers at businesses with fewer than 100 employees, and 67% of all private-industry workers, had access to a workplace retirement plan (Bureau of Labor Statistics; *Employee Benefits in the United States*; Table 2; March 2020).

2 For additional information on these programs, see the Academy issue brief, *State-Based Retirement Initiatives and the AGES Principles* (November 2017).

IRA programs lack many features and benefits that 401(k) plans and other qualified defined contribution (DC) plans offer (e.g., employers generally cannot make matching contributions into IRAs, and IRAs have lower contribution limits than qualified DC plans).[3]

Enter the SECURE Act, signed into law in December 2019. Among its various provisions, one that may have a significant impact on retirement security is the establishment of the Pooled Employer Plan (PEP), effective January 1, 2021.[4] PEPs allow multiple, unrelated employers of any size to participate in a single retirement plan that is a defined contribution plan qualified under Internal Revenue Code section 401(a).[5]

The intent behind PEPs is to expand retirement plan coverage among (primarily smaller) employers that have not adopted a plan for the reasons noted earlier (i.e., cost, liability exposure, and compliance and administrative burdens). PEPs have the potential to be less expensive than single-employer DC retirement plans, limit liability, and enable employers to outsource most of the compliance and administrative efforts associated with operating retirement plans. PEPs might also offer some features that an employer might not choose to offer through their single employer plan such as insured and/or non-insured retirement income options. It is also possible that some employers that already sponsor plans may switch over to PEPs to lower their cost of compliance, to reduce administrative and operational duties, and to transfer some of the fiduciary risks associated with managing their own plans. However, it is too soon to know whether or how many sponsors might elect to switch.

Prior to the adoption of PEPs, individual employers could join together only in a multiple employer plan (MEP). However, MEPs could only be joined by employers that share a common business element or as part of the same professional employer organization (PEO). Another downside of MEPs is referred to colloquially as "the one bad apple rule."

3 In 2021, the IRA contribution limit is only $6,000 ($7,000 at age 50 or older), while in a 401(k) plan, an individual can contribute up to $19,500 ($26,000 at age 50 or older) on a pre-tax or Roth basis and the total of employer and employee contributions can be up to $58,000 (prior to the $6,500 additional amount at or after age 50).
4 An Academy issue brief on the potential impact of the SECURE Act on retirement security is available here.
5 PEPs can also be structured based upon Individual Retirement Accounts.

Members of the Retirement System Assessment and Policy Committee, which authored this issue brief, include Eric Keener, MAAA, FSA, FCA, EA—*Chairperson*; Claire Wolkoff, MAAA, FSA—*Vice Chairperson*; Kelly Coffing, MAAA, FSA, EA; David Driscoll, MAAA, FSA, FCA, EA; Lee Gold, MAAA, ASA, EA; Scott Hittner, MAAA, FSA, FCA, EA; Cynthia Levering, MAAA, ASA; Esther Peterson, MAAA, ASA, EA; Andrea Sellars, MAAA, FSA; and Mark Shemtob, MAAA, FSA, FCA, EA.

Under this rule, if just one of the participating employers causes the plan to violate the rules and regulations applicable to tax-qualified plans under ERISA[6] and the Internal Revenue Code, the entire plan could face disqualification. PEPs are not subject to "the one bad apple rule," nor is there any requirement that employers joining a PEP have any common business element.

Under the SECURE Act, an entity must be a "Pooled Plan Provider" (PPP) registered with the U.S. Department of Labor (DOL) and Department of Treasury in order to offer a PEP to employers. The PPP is the named fiduciary of the PEP, acts as the plan administrator, and ensures that all parties handling plan assets are bonded. A PPP can be a third-party administrator, insurance company, mutual fund management firm, broker-dealer, or even an individual. As of this writing, dozens of organizations have registered with the DOL as PPPs, and the number is expected to continue to grow. The increasing number of potential providers highlights the challenges that plan sponsors will face in choosing whether to participate in a particular PEP. These challenges may be particularly significant for smaller plan sponsors lacking the resources and expertise to support the decision-making process.

Employer Considerations

The Employee Benefits Security Administration (EBSA) of the DOL has issued final registration requirements for PPPs. This final rule establishes a new form, EBSA Form PR, which must be filed no later than 30 days before the operation of a PEP by a PPP. The form requires information needed by the DOL to identify, contact, and engage in timely oversight of PPPs, as well as information that the DOL could post on its website that would provide employers, employees, and other interested stakeholders with the ability to identify, contact, and perform due diligence on PPPs. Though the registration includes a description of the administrative, investment, and fiduciary services that will be offered, including a description of the role of any affiliates in such services, it likely will not provide sufficient information for an employer to assess whether a particular PEP is a good choice for its employees or to compare alternative PEPs.

Below are some considerations employers may address when trying to decide whether to participate in a particular PEP. There will be many PEPs available in the market from which to choose; thus, employers will need to look to a PPP's and/or a PEP's marketing or other materials for more detailed information. But, what essential information would employers seek and consider?

6 Employee Retirement Income Security Act of 1974 (ERISA).

What might an employer consider in choosing whether to participate in a PEP?

While a PEP has promise in reducing administrative and operational burdens, the employer may lose flexibility with respect to certain plan design features and choice of service providers. These trade-offs may be acceptable if the benefits of moving to a PEP outweigh the loss of flexibility. While the PPP takes on fiduciary responsibility for the PEP, the employer still has the duty to select and monitor the PEP including the PPP.

Some key areas an employer may consider include:

1. The magnitude of the reduction, if any, in administrative costs as compared to sponsoring an individual plan.
2. The level of investment-related expenses. For example, institutionally priced investment options are currently available at low minimum balances for many index funds, so investment-related fees for those funds would be unlikely to be reduced significantly.
3. The employer cannot transfer all administrative responsibility. For example, the employer would likely retain at least some responsibility for:
   a. Providing accurate participant data
   b. Accurately determining plan compensation and contributions based on plan terms
   c. Withholding the proper funds
   d. Remitting contributions in a timely manner
4. As fiduciaries, employers would still need to monitor their PPP and other vendors if applicable.

What might an employer consider when selecting a PEP?

Once an employer has made the decision that a PEP is a good option for the organization, the specifics of the various PEPs offered become important. What follows is a list (not exhaustive) of employer considerations regarding specifics of a particular PEP. Employers that already maintained plans may approach the decision of selecting a PEP based upon the specific features being offered such as the ability to transfer or roll over assets to the PEP.

<u>Investment Choices:</u> What investment choices are available? What is the default fund(s) if employees do not make an election? Are the investment-based fees and expenses reasonable based upon the services being provided? Is it easy for individuals to make investment selections that best suit their needs and goals? Can employers offer additional investment options if they so choose? Are managed account services an option?

Administrative Services and Fees: What administrative services does the PPP provide? What are their technological capabilities? How will they coordinate with the employer's payroll provider and possibly other service providers? How will the PPP manage lost participants, uncashed checks, forfeiture accounts, etc.? What are the fees charged? Who pays the administrative fees—the employer or employee? Does the employer have flexibility in allocating these fees? Are the fees competitive based on the services provided? Are all investment fees readily and fully disclosed?

Participation Features: How do employees sign up for the PEP? Does the PEP offer a default contribution option? Does the PEP support both pre-tax and Roth contributions? How do employees make investment choices?

Employer Contributions: Does the PEP allow for employer contributions? If so, what types are available—matching, non-matching, or both? Must the employer contribution options be fixed, or can they vary based on various factors (e.g., employer profits)?

Retirement Income Options: Once an employee retires, what options are available to withdraw funds? Does the PEP allow for the purchase of lifetime income products from insurers, and, if so, which insurers and what options are available? Does the PEP allow for non-insured structured retirement income payouts, and if so, which ones? How do they offer participants support for required minimum distributions?

Long-Term Retirement Planning: What information is provided to help employees know whether they are on track to meet their retirement goals? Is there a tool available through which employees can perform their own modeling based on alternative assumptions such as level of future contributions, target retirement ages, and investment alternatives and returns?

Portability: Does the PEP permit the transfer of funds from a prior plan or rollover IRA? Can an employee easily arrange such a transfer? When an employee changes jobs, is it easy to roll over funds from the PEP to another plan or rollover IRA if desired?

Retirement Education: What type of retirement education is offered to employees? How is it provided? Does education vary by the stage of the employee's working career? Can it be tailored to a particular employer's workforce? Does the plan offer assistance to individuals as they decide among lifetime income options, lump sums, or other distribution options?

Retirement Advice: Does the PPP offer advice to employees near retirement and, if so, who provides the advice and how is it paid for?

Conflicts of Interest: Are there companies/service providers affiliated with the PPP that are providing services or investment options for the PEP? What are the relationships among the PPP, the recordkeeper of the PEP, and the investment managers offering funds within the PEP? Are the relationships clear and fully disclosed?

What is the business structure of the PPP?

As noted above, a PEP is offered and managed by a PPP. The actual PPP would in many cases impact the PEP selection as a result of name recognition or an existing business relationship. Some employers may also be more comfortable selecting a PEP where the PPP is a specific business structure, such as a financial institution or an insurance company, without delving into the specific provisions of the PEP offering. The selection of the PEP as well as periodic monitoring as to whether it remains appropriate (both the PPP and specific PEP provisions), are fiduciary requirements that the employer cannot avoid, thus initial and ongoing due diligence is critical.

Conclusion

As discussed above, there are many important issues that employers would need to consider as they determine whether to offer a PEP to their employees and decide to select a particular PPP. Not all of these issues are equally important to every employer. For many small employers, analyzing the above considerations can be challenging, and a third-party adviser may be helpful to assess which options would best meet the employer's and their employees' needs.

Time will tell how PEPs and their PPPs impact the retirement landscape in the U.S. However, the SECURE Act offers the potential for expanded retirement plan availability and improved retirement outcomes to smaller employers and their workers.

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