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MORNINGSTAR

One Man's Story of the Origins of ERISA

September 2, 2010(https://fiduciary-experts.com/2010/09/02/)

W. Scott Simon

President Gerald Ford signed the Employee Retirement Income Security Act into law on Sept. 2, 1974–36 years ago on the publication date of this month's column. Among those sitting in the audience in the East Room of the White House that day witnessing this historic event was Jeffrey Mamorsky, a young attorney for Mobil Oil. Mamorsky was invited to the signing ceremony because he played an important part in educating and advising the congressional staffs that drafted ERISA. But how did an attorney for an oil company who wanted to grow up to be a sportswriter wind up in the White House that day, smiling and happy that this great law had finally been enacted and now signed into law?

Many of us deal with qualified retirement plans in our profession every day. Some even become engrossed in the intricacies of the laws of ERISA, the Internal Revenue Service and the U.S. Department of Labor, and the regulations thereto. Very few of us, however, really know the story behind ERISA, and how and why it came into being. So I thought it might be interesting over the next few months to explore the historical antecedents of modern qualified retirement plans in America and in the process record the oral history, so to speak, of one person who played an important role in shaping the world that many of us inhabit in our professional lives today.

I recently interviewed Mamorsky, who is now co-chairman of the Global Benefits and Compensation Group at Greenberg Traurig, LLP, an international, full-service law firm with 1,800 attorneys in more than 30 offices in the United States, Europe and Asia.

Scott Simon: Thanks for consenting to this interview, Jeff. I'm sure that many people will find it interesting and enlightening.

Jeff Mamorsky: Glad to be with you.

Did you always want to grow up and be a lawyer?

No. At first I wanted to be a sportswriter. I always loved writing. From the time I was 16, I had to support my mother and my younger brother. I started out writing for the school newspaper in junior high. After that, I managed to work my way through high school, college and law school as a sports writer. I worked for the New York Times, the New York Daily News and the Herald Tribune, and I actually did pretty well; I made about $60 a week and this was in the late 1950s, early 1960s, doing that.

Where did you go to college?

I went to NYU when they had an uptown campus in the Bronx in University Heights, because they had the best college daily newspaper in the United States, the Heights Daily News–other than Columbia. When I graduated from college, I wanted to go to Columbia journalism school and get my master's degree. But even though I got in, I didn't get a scholarship. I was really disappointed because that's what I really wanted to do, to be a sportswriter.

So what did you do then?

Well, I got a scholarship to law school. My college dean told me I would be a good lawyer because I was a good writer and I liked to do research. So I went to law school at the University of Buffalo but after only one year there, I was drafted by the Army during the Viet Nam war. After I got out of the Army, I looked for a job pending my return to law school. I saw an ad in the newspaper, went to the employment agency, and lo and behold there was my old fraternity brother from college. He said that he had the perfect job for me at Prentice Hall as a legal editor. The only problem was that I was not yet a lawyer but he sent me over there anyway even though I hadn't yet graduated from law school. I got the job but after a couple months, the personnel department contacted me and said, "Mr. Mamorsky, we don't have your transcripts from law school," and I said "Well, I still have to finish law school." Well, that caused a stir and they were going to fire me, but my immediate boss said there was no way you are going to fire Jeff, he's the best writer we have ever had here.

So you're in your first job after getting out of the Army and within a few months, they're already ready to fire you?

Yes. So I guess there was a compromise with those who wanted my scalp. One, they punished me by lowering my salary from $9,000 to $5,000 a year. And two, they reassigned me to the pension and profit sharing department which published legal loose-leaf services updated on a weekly basis in the benefits and compensation area.

So let me get this straight: after finding out that you weren't a law school graduate, Prentice Hall was going to fire you but they relented at your boss's insistence but not without punishing you by lowering your annual salary nearly 50% and assigning you to pensions.

Yes, that's about right; crazy, isn't it! Now remember, this was in 1967 and at that time there were only two legal loose-leaf services–one was Commerce Clearing House and the other was Prentice Hall. That was obviously prior to ERISA and lawyers didn't really do any pension stuff then. Pension work was really done by actuaries and insurance companies, and the only lawyers that were really involved were the people at Prentice Hall and Commerce Clearing House. So I had the good fortune of being a legal editor at Prentice Hall in 1967–except that I was not yet a lawyer!

Were there any people that really helped educate you about pensions?

Yes, two in particular. One of the people that helped me out greatly was a gentleman by the name of Leo Brown who was the pension chief of the IRS in Manhattan. In the late 1960s, early 1970s, most Fortune 100 companies were headquartered in Manhattan so Leo was a very important guy. In my first month on the job at Prentice Hall, the IRS came out with some tandem stock options rulings. I didn't know what I was doing so my boss told me to call Leo Brown and that he would help me out. I expressed some reservation in calling the pension chief of the IRS but I summoned up the courage and called him anyway, and surprisingly he took me under his wing. Leo helped me a great deal, really taught me pensions. Leo then introduced me to Isidore Goodman who, prior to ERISA, was the IRS pension chief of the entire country. That's no exaggeration; I mean when he made a speech, it was tantamount to a revenue ruling. Mr. Goodman asked me to cover and publish all his speeches for the Prentice Hall Pension & Profit Sharing publications. Eventually I traveled to Washington DC more and more, I got to be known as the person who was close to the IRS and who knew Isidore Goodman, and also Leo Brown.

My understanding is that what really kicked off the movement to reform pensions in America was closure of the last Studebaker Motor Company manufacturing plant in 1963. Upon termination of the Studebaker pension plan on October 15, 1964, current retirees and retirement-eligible employees over the age of 60 received their full pension, vested employees under the age of 60 received about 15% of their pensions and non-vested employees, including everyone under 40, received 0%.

Sadly, that was true. Prior to ERISA, a non-bankrupt employer could legally terminate a pension plan without funding all vested benefits. In the old days, there were no rules as we know them today whatsoever. There were labor laws under the 1947 Labor Management Relations Act [informally known as the Taft-Hartley Act] but they really didn't do very much at all. The Act said only that it was legal for a union to set up a pension plan as long as you had a joint board of trustees consisting of both management and labor. The reason why Studebaker caused such a huge brouhaha was that in those days there was no vesting until you retired. I know that it sounds absolutely crazy now but that's how it was. The only real regulations then were found in the qualification rules of the Internal Revenue Service that had been in place since 1928. There were also interpretations by Isidore Goodman through his speeches, and through revenue rulings, but they basically related only to maintaining the qualification of a pension plan through compliance with the tax laws. There weren't any vesting rules, eligibility rules, survivor rules, break in service rules or any of the other things we know today. And most unbelievably, there weren't any fiduciary rules at all! Now even though the Studebaker plant closing happened in 1963, before the time I got into pensions, it still wasn't until around 1968 that any bills were introduced in Congress to reform pensions. Since I was the legal editor at Prentice Hall in charge of pensions then, I was responsible for covering the congressional hearings and writing about them.

Who pushed these reforms in Congress?

There were four gentlemen who were the greatest proponents. The most important one was Senator Jacob Javits from New York and I got sort of friendly with him over the years. Jack–that was the first name he went by–Javits was just passionate about passing legislation to protect the workers with regard to their retirement benefits. Jack Javits was a great man, a real icon. And there was Senator Harrison Williams – Pete was the first name he went by – from New Jersey who was also passionate about pension reform and a great man. Then on the House side, there were John Erlenborn from Illinois and John Dent from Pennsylvania, who also were very, very, passionate. So you had four gentlemen that were just driven to get these laws passed. But even though these bills started to float around beginning in 1968–with Jack Javits really the one that started it all–things really didn't start to happen until 1972. That was lucky for me because at that point in time Mobil Oil asked me to join them. I had been at Prentice Hall from 1967 to 1972, I finished law school at night and I also got my LLM in tax from NYU law school at night. Prentice Hall paid for my education, so it was just great, it was a phenomenal experience. To this day, I still count my lucky stars for my association with Prentice Hall.

So what drew you to Mobil Oil?

Well, first I have to tell you that I didn't even plan to join Mobil. I had an offer from a major law firm and wanted to take that. But my mentor, Leo Brown, encouraged me to join Mobil because lawyers didn't do pensions then, and Leo told me that if you really want to learn about pensions, you should go to a company like Mobil because it was really a leader in the employee benefits area. Mobil at that time was No. 3 in the Fortune 100, and it was the first company to ever do a savings plan which was a precursor to the 401(k), and the first to do a 501(c)(9) cafeteria plan. There was a brilliant guy there by the name of Bob Lane and he was one of the first great pension benefits lawyers. He was working in-house and he was about to retire so they were looking for someone to take over his job and be the benefits and compensation counsel at Mobil.

Tell me about your experiences at Mobil.

Well, one early experience at Mobil taught me the importance of a lawyer being "solution driven" rather than just seeing limitations and telling a client "No." Mobil was in the process of buying a pipeline company from another large oil company. Pete Krist the executive vice president of employee relations summoned me to his office and told me that Mobil hoped to receive a highly favorable tax treatment on the deal. I told him that two revenue rulings were just issued by the IRS that did not permit favorable tax treatment [both are still in force today]. I felt it was my job to give him solid, accurate legal advice so I said "I'm sorry, Mr. Krist, but based on those revenue rulings we just cannot do it." He looked at me and turned bright red and then he said, "Mamorsky, how long have you been with Mobil?" And I said, one month sir, and he looks at me and says, "you better figure this out." So I went to work and found a way to get favorable tax treatment. I bounced it off Leo and he said it worked. That's when I became solution driven.

So I guess the favorable tax treatment of that pipeline deal made Pete Krist a happy camper?

Well, after solving the problem, I called Krist and went back up to his office. I told him that I got it done, and he was so impressed, he was just blown away. He mentioned what I had done to the chairman of the board of Mobil Oil, Rawleigh Warner Jr. They were both very impressed with what I had done because it was their experience that lawyers aren't very solution driven. As a result, Warner, who was also then chairman of the Business Roundtable, asked me to become counsel to a Business Roundtable Taskforce that had just been established to review the various pension reform bills that were then being introduced in Congress. This Business Roundtable Taskforce was actually the precursor to the ERISA Industry Committee–known today as ERIC–which is the leading representative of large companies in the benefits and compensation area today. I provided input to Mobil and the other companies in the Business Roundtable Taskforce and by doing so, I began working with the House Pension Task Force and the Senate Finance Committee in looking at the bills. And that lead to my going to Washington to help draft ERISA.

My interview with Jeffrey Mamorsky will continue next month.

W. Scott Simon is an expert on the Uniform Prudent Investor Act, Restatement (Third) of Trusts and Title I of ERISA. He provides services as a consultant and expert witness on fiduciary investment issues in depositions, arbitrations and trials as well as in written opinions. Simon is the author of two books including The Prudent Investor Act: A Guide to Understanding. He is a member of the State Bar of California, a Certified Financial Planner® and an Accredited Investment Fiduciary Analyst™. The author's views expressed in this article do not necessarily reflect the views of Morningstar.

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One Man’s Story of the Origins of ERISA (Part 2)

September 2, 2010(https://fiduciary-experts.com/2010/09/02/)

W. Scott Simon

In this month’s column, I continue my interview with Jeffrey Mamorsky. Here is Part 1 (http://advisor.morningstar.com/articles/article.asp?docId=20203).

Scott Simon: So you became legal counsel to a Business Roundtable Task Force, which had been established to review the various pension reform bills that were being introduced in Congress in the early 1970s?

Jeff Mamorsky: Yes, that’s right. As counsel to a task force of lawyers from representative Business Roundtable companies, which was the precursor to the ERISA Industry Committee–known today as ERIC–I began working with the House Pension Task Force and the Senate Finance Committee in looking at the bills. And that led to my going to Washington to help draft ERISA.

So were you one of the principal drafters of ERISA?

Oh, no. ERISA was drafted principally by the staffs of Sen. Javits, Sen. Williams, Congressman Dent, and Congressman Erlenborn. I worked with the staff members and the congressional committees, and helped provide input to them. Don't forget that in those days there really weren't too many people with experience in running retirement plans. I was just lucky to be one of the few. I had the experience working at Prentice Hall and then working at Mobil, which had a huge benefit plans administration department, more than 100 people. While at Mobil, I worked with best-of-class benefit professionals such as Bob Peters, who was director of benefits, Art Foli, who was manager of benefit plans administration, and a brilliant in-house actuary, Ed McGarrity. So with the great team at Mobil and the other companies on the Business Roundtable Task Force, we were able to educate Congress in the pension legislation process. But it was educating the four gentlemen who were responsible for the ERISA statute and their staff people that was really our most important work.

Why are Title I and Title II of ERISA so much alike?

There were tandem pension bills moving through at the same time on both the House side and the Senate side. You had a House and Senate labor committee, and then you had the House and Senate tax committees, and they could never agree on things. Don't forget, this was very volatile, cutting-edge legislation then. Title I of ERISA is the labor title and Title II is the tax title–or really the employee benefits requirements of the Internal Revenue Code–and they are pretty much in almost all respects parallel statutes. If you put them side by side, you will see that eligibility, funding, and vesting are all pretty much parallel. Even in the prohibited transaction rules, you have the labor titles where the Department of Labor can impose civil penalties, and you have the tax title, where the IRS can impose excise taxes. And that's why Title I and Title II of ERISA are so much alike.

Do you know who came up with the name “Employee Retirement Income Security Act”? That's quite a mouthful and I was curious as to its origin.

I actually think that it was Sen. Javits who came up with the name, since he was the one who was the real catalyst of the pension reform effort. Sen. Javits was just a great man, having led the pension reform effort for many years conducting Senate hearings on the “broken pension promise” since the

Studebaker plant closing in the early 1960s.

As you may know, there is a lot of debate going on now about the value of independent fiduciaries in qualified retirement plans.

Oh, yes, I'm very familiar with that debate and, in fact, have a great deal of personal experience with independent fiduciaries in qualified retirement plans since, among other things, I'm legal counsel for the largest multiple employer plan in America.

Later in our interview, I'd like to discuss independent fiduciaries in-depth, especially what value they bring to multiple employer plans (MEPs), but for now, could you please comment on them in general?

Well, the investments and operations aspects of a plan simply work better with independent trustees. The best way to run a plan is with an independent fiduciary, and the simple reason why is because that gets rid of all the conflicts inherent in running a retirement plan.

Your mention of independent fiduciaries gives me a good segue way into the great emanating idea of ERISA, which explains why it's structured the way it is. Look, I was a lawyer working on the business end, employed by Mobil, and legal counsel to the Business Roundtable Task Force. It was extraordinarily important to business to be sure that, whatever form ERISA took, companies would be involved in running their retirement plans. That made sense because the contributions made by businesses to defined benefit plans on behalf of employees–remember, no 401(k) plans existed then–was company money–well, at least before it landed in the plan. So companies really wanted to be sure that they would be involved in helping run their plans. This notion, of course, is completely contrary to how everyone else in the world operates their pension systems! They have separate trustees, independent trustees. The United States is the only country in the world where the employer plan sponsor can be a fiduciary of a pension plan. In all other countries, you have to have independent fiduciaries, independent trustees. In Europe, for example, employers can't get involved with retirement plans at all.

Could you please comment more on the "great emanating idea of ERISA"?

Yes, the rules for ERISA all emanate from the fact that they represent a grand trade- off for allowing companies to be able to run and control their retirement plans. If you're going to have companies run their employee benefit plans, pension plans, you obviously have an inherent potential conflict of interest. Our issue, then, the work I was doing for the Business Roundtable, was to convince the government that we could, in fact, put in the proper fiduciary structures and rules that would make sure that any employer, when they're wearing their hat as a fiduciary to their plan–as opposed to wearing their hat as a fiduciary to their stockholders–would do their job prudently.

One result of this, for example, was the basic fiduciary rule that was drafted under ERISA section 404(a)(1)(A): to act solely and exclusively for plan participants. That's why the words "solely" and "exclusively" are in there, because an employer, or a designee of an employer such as an officer or a committee appointed to run the plan, even though they're working for the company, once they are a fiduciary of the plan, they have to act solely and exclusively for plan participants. So if there is any discretionary decision whatsoever, it has to be weighed in favor of the plan participant because of the exclusive benefit role. Also included in 404(a) is that fees have to be reasonable for the same reason, to protect plan participants.

So the basic structure of ERISA was built on this very delicate balance between businesses wanting to control their retirement plans and the requirement that they must be fiduciaries acting solely and exclusively in the interests of the participants in those plans?

Yes, that basic trade-off is what resulted in today's ERISA's fiduciary responsibility requirements, which are very complicated but were very exquisitely drafted. These requirements are obviously very stringent. For example, the prohibited transaction rules make you guilty before you get the chance to prove your innocence. Under ERISA section 406 (Title I) and IRS section 4975 (Title II), any transaction between a plan and a party in interest or a disqualified person under the code, anything directly or indirectly–for example, even a service provider receiving money from a plan–is a prohibited transaction, unless you fit into a statutory exemption or a regulatory exemption like a class exemption. One well-known exemption is ERISA section 408(b)(2) which is a statutory exemption to the prohibited transaction rule. We wanted to make sure that anybody working at the employer level–irrespective of a title–that had any discretion or any advisor that had any discretion would be a fiduciary. That's why ERISA section 3(21)(a) is so very broad, utilizing a functional fiduciary test. All these rules–the exclusive benefit requirements, the prohibited transaction rules, the self-dealing rules and others–are incredibly onerous because of all the conflicts that can occur in a retirement plan. Frankly, if these rules were all followed properly, we wouldn't have any Enrons and other such disasters that have devastated plan participants.

What role did labor play in all this?

Labor wasn't involved at all because there was a decision made early on that multiemployer plans, union plans, were so poorly funded and so poorly run that they shouldn't be part of ERISA. In the years prior to the enactment of ERISA in 1974, the decision was made that we just couldn't deal with multiemployer plans because it was bad enough trying to enforce corporate retirement plans! Multiemployer plans weren't subject to the ERISA statute until 1980, when the Multiemployer Pension Plan Act of 1980 was enacted. So it's important to recognize that in the negotiation process of ERISA, we were dealing only with companies not labor unions. In my view, if labor unions had been involved from the get-go in the legislative process in the early 1970s, you probably would have had independent trustees incorporated into ERISA. Because under the Labor Management Relations Act of 1947–also known euphemistically as the Taft-Hartley Act–it was always a rule to have a board of trustees made up of an equal number of labor and management. So if the original ERISA legislation had included multiemployer plans, we probably would have had independent trustees because plans work a lot better with independent trustees. They just do because conflicts are avoided.

Note: I stated mistakenly in last month's column that ERISA was signed into law by President Gerald Ford in the East Room of the White House. The Rose Garden is where the ceremony actually occurred. However, a smaller, more private signing ceremony did take place in the East Room.

My interview with Jeffrey Mamorsky will continue next month.

W. Scott Simon is an expert on the Uniform Prudent Investor Act, Restatement (Third) of Trusts and Title I of ERISA. He provides services as a consultant and expert witness on fiduciary investment issues in depositions, arbitrations and trials as well as in written opinions. Simon is the author of two books including The Prudent Investor Act: A Guide to Understanding. He is a member of the State Bar of California, a Certified Financial Planner® and an Accredited Investment Fiduciary Analyst™. The author's views expressed in this article do not necessarily reflect the views of Morningstar.

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One Man's Story of the Origins of ERISA (Part 3)

November 4, 2010(https://fiduciary-experts.com/2010/11/04/)

W. Scott Simon

In this month's column, I continue my interview with Jeffrey Mamorsky. Here is Part (http://advisor.morningstar.com/articles/article.asp?docId=20203) *1* (http://advisor.morningstar.com/articles/article.asp?docId=20203).***;*** *part two is here* (http://advisor.morningstar.com/articles/article.asp?docId=20459&email=pb1006A3).

Scott Simon: Jeff, I'd like to pick up on a point that you made earlier in the interview. You said that qualified retirement plans such as 401(k) plans work a lot better when independent fiduciaries are in charge of running them.

Jeff Mamorsky: Yes, that's right. One good example where independent trustees can make a real difference is in a multiple employer plan. There is a basic, critical difference between a multiple employer plan and other qualified retirement plans such as 401(k) plans. In your typical 401(k) plan, the employer and the plan sponsor are one and the same so company X is the plan sponsor. That makes the employer and the board of directors of the employer responsible and liable. But in a MEP, the sponsor of the MEP is not the employer but a separate and distinct entity from the employer. The sponsor of a MEP assumes all the duties that are inherent in a non-MEP such as those of the Named Fiduciary and Plan Administrator. On the one hand, the sponsor of the MEP could choose to reserve all these duties for itself. On the other hand, that sponsor, just like in a non-MEP, could choose to delegate all such duties to an Independent or Managing Fiduciary as the designated Named Fiduciary for plan investments and administration. The Independent Fiduciary could, in turn, choose to retain all such duties for itself or it could delegate them to the other designated fiduciaries. It's important to remember, though, that at each stage of delegation in a multiple employer plan, like in a non-MEP, there's a corresponding monitoring duty charged to the entity making the delegation. So while the sponsor of a multiple employer plan ordinarily is solely responsible and liable for managing all plan service providers and ensuring that the plan operates according to the plan document and all ERISA, IRS and DOL requirements, it does have the option to delegate to others some of those responsibilities and liabilities with appropriate monitoring oversights in place. This helps to diversify fiduciary responsibility and reduce risk further.

So what are the primary advantages of a multiple employer plan?

An employer that decides to join a MEP gets cost efficient administration and investments for its employee participants, and also has the assurance that the plan is being run by a professional in accordance with ERISA's prudent expert rule. However, it is important to emphasize that the employer's due diligence in selecting a well-run MEP is critical. A good indication of this is a MEP which is run by an Independent Fiduciary professionally accredited by the Independent Fiduciary Guild and Fiduciary Audit Protection Program. These are advantages for both the employer and the employees. But the greatest advantage by far for the employer in joining a multiple employer plan is that it avoids fiduciary responsibility and liability because most MEPs are run by a governing body of Trustees or Named Fiduciaries as Plan Sponsor with no involvement by any adopting employer. In this regard, it is important to review the MEP plan document and Adoption Agreement to make sure that the employer has no residual fiduciary responsibility.

Is an employer's decision to join a MEP fiduciary in nature or is it simply a settlor decision which would be non-fiduciary in nature?

No, it's just a settlor decision, it's not fiduciary in any way. From a legal standpoint, the employer is merely adopting the MEP which is a settlor decision. The running of the plan is fiduciary in nature and, as mentioned earlier, it's the plan document and adoption agreement which need to be carefully examined to make sure the employer has no fiduciary responsibility in running the plan.

So once an employer has chosen to join a multiple employer plan, does it sort of yield to the sponsor of the MEP?

Not sort of yield, it yields entirely, to the sponsor if the plan is drafted correctly. Once an employer joins a multiple employer plan, all fiduciary responsibilities and liabilities are given up by the employer to the sponsor and whoever the sponsor has named– typically an Independent Fiduciary–to run the MEP which has an existing fiduciary infrastructure. This includes even settlor issues such as amending the plan. By the way, that doesn't have to be the case, but it's normally the case. You can have a multiple employer plan where you have member employers of a trade association in a certain industry that want to have representatives of the employers serving as the Named Fiduciaries of the MEP. But even in that kind of situation, it's important to remember that the representatives are in no way there as employers but as Named Fiduciaries appointed by the sponsor of the MEP to run the MEP.

Once an employer has made the decision-settler in nature-to join a multiple employer plan, does it still retain any monitoring duties?

That's a very good question. Let me be clear: an employer retains no monitoring duties whatsoever once it has joined a multiple employer plan. The only responsibility that an employer retains is to make sure that its employees get enrolled and that contributions are made on time. Both of those functions are ministerial acts, settlor in nature, not fiduciary acts. Now, within a multiple employer plan, there are plenty of monitoring duties that must be carried out but those duties are borne by the sponsor of the MEP and any fiduciaries it may appoint, but not by any employer that has decided, on a settlor basis, to join the MEP.

You've said that a multiple employer plan is considered to be a single employer plan under the law. Could you please explain that seeming paradox?

Sure. We never thought of a multiple employer plan in the early days of ERISA as anything other than the plan of a controlled group. For example, let's say that Mobil had 20 subsidiaries and each subsidiary adopted a "jumbo plan" with 20 companies in that plan, or 20 different types of benefits. There really weren't any multiple employer plans with unaffiliated companies in the plan. MEPs have always been considered to be a single employer plan under the law; I know that sounds strange but that's how it is. So the best way to consider the seeming paradox is that a multiple employer plan is a single employer plan that is simply utilized by multiple employers. In a MEP, there is only a single sponsor of the plan, one plan document, one record-keeper, one custodian, etc. Other subsidiaries or unrelated businesses may join and then yield to the fiduciary infrastructure of the multiple employer plan.

You just mentioned that other subsidiaries or unrelated businesses may join a MEP which brings to mind the explanation I provide to plan sponsors that are considering joining a MEP. I tell them that, at first, different divisions of one company could form a MEP, then the concept of a MEP expanded to include different companies in the same industry such as trade associations and then the concept of a MEP expanded further to include different companies in different industries. I stress that the law has never changed–it was the same in 1974 when ERISA was enacted as it is today–just the concept of the nature of the relationship between the entities that can join a MEP.

Yes, I would agree. That's an accurate explanation. You would naturally think, for example, of a multiple employer plan as being comprised of companies in the same industry such as a trade association but there's no legal requirement that it be in the same industry.

Some ERISA attorneys are uncomfortable with a multiple employer plan because they say that one sour apple employer in a MEP could taint all the other employers and result in disqualification of all the plans in the MEP.

You can have a multiple employer plan with defined contribution or defined benefit plan features. On the defined contribution side, you have virtually no chance that a bankrupt employer will impact the other participating employers since participants in the DC plan each have individual accounts and are not at risk of losing everything when an employer goes bankrupt. However, if an employer goes bankrupt on the defined benefit side, the other employers in the MEP become responsible for paying the DB benefits of the employees in the bankrupt company. Moreover, in both a DC and DB plan if an employer commits a disqualifying defect, the entire DC or DB MEP can be disqualified under the rules of ERISA section 413. That's why you need to monitor a multiple employer plan very carefully to make sure that the plan is operated in accordance with plan documents and all applicable law (ERISA and IRS requirements) and that an employer is not committing an operational defect and otherwise causing the plan to be in violation of ERISA or IRS rules. It's incumbent on those who are running MEPs to establish best-practice operational internal controls, funding structures and other prophylactics to ensure that if one employer is not cooperating with the plan or it goes belly up, the other employers won't get hurt. With respect to funding, you can do that by setting up withdrawal assessments, so if a company wants to play games and withdraw from a MEP they get hit with a contingency assessment. It can also be achieved by making sure that every employer is funding properly. Also, with regard to protecting the plan under ERISA and DOL requirements for the MEPs that I represent, I place a "disgorgement" provision in the plan and trust documents that remove employers who are found to be committing disqualifying defects. I also perform Fiduciary Audit® Operational Reviews and constantly monitor, and if I find an employer that is recalcitrant and will not agree to correct defects that I've uncovered, then whoever is running the MEP can throw that employer out of the plan in accordance with the plan document I've drafted.

But is it possible even under your best practices monitoring system that you could miss a rotten apple in the barrel that could still taint the whole MEP?

No, not if you monitor. You would go in and do self audits to make sure that a multiple employer plan is being run properly. In addition, the IRS audits MEPs. The IRS would want to see if there are internal controls at the level of whoever is running the MEP. The Plan Sponsor or Independent Fiduciary has to have controls in place with all the employers in the MEP to make sure that the employers are sending the right information to the plan administrator such as making sure that the company payroll is correct, as well as eligibility and service. That should be done quarterly.

It sounds like a multiple employer plan is the best thing since sliced bread.

A multiple employer plan is an excellent plan particularly if it’s a defined contribution individual account plan, but only if it’s run by a Plan Sponsor or Independent Fiduciary who are experts in plan investments and administration. An employer needs to be cautious in adopting a defined benefit MEP with dozens or even hundreds of other companies, especially in this economically volatile environment, because there is the possibility that other companies may go bankrupt and the remaining employers will have to make plan contributions for employees of the bankrupt employers. Running a multiple employer plan properly is a great challenge which is why a MEP really needs the right expert Plan Sponsor, Independent Fiduciaries and other plan advisors.

My interview with Jeffrey Mamorsky will conclude next month.

W. Scott Simon is an expert on the Uniform Prudent Investor Act, Restatement (Third) of Trusts and Title I of ERISA. He provides services as a consultant and expert witness on fiduciary investment issues in depositions, arbitrations and trials as well as in written opinions. Simon is the author of two books including The Prudent Investor Act: A Guide to Understanding. He is a member of the State Bar of California, a Certified Financial Planner® and an Accredited Investment Fiduciary Analyst™. The author’s views expressed in this article do not necessarily reflect the views of Morningstar.

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One Man's Story of the Origins of ERISA (Part 4)

December 2, 2010(https://fiduciary-experts.com/2010/12/02/)

W. Scott Simon

In this month's column, I conclude my interview with Jeffrey Mamorsky. Here is part one (http://advisor.morningstar.com/articles/article.asp?docId=20203)*; part two* (http://advisor.morningstar.com/articles/article.asp?docId=20459)*is here; and here's part three* (http://advisor.morningstar.com/articles/article.asp?docId=20650).

Scott Simon: Jeff, some of what I've written about in this column over the past year or two concerns the poor governance practices of even very large companies that sponsor 401(k) plans such as the investment options they offer to plan participants like retail mutual funds. It seems to me that even many Fortune 500 companies, much less mom-and-pop operations, just don't know what they're doing in running their 401(k) plans. Am I way off base here?

Jeffrey Mamorsky: No, not at all. But before going any further, let me go back to the basic fundamentals of ERISA. It's the board of directors of the company sponsoring a 401(k) plan that has the ultimate legal responsibility for the plan. That's ERISA 101. But in drafting ERISA we knew that boards of directors ordinarily would not be focused on the plan even though they are plan management fiduciaries and have personal liability under ERISA. However, ERISA provides a number of ways in which a board may allocate and delegate fiduciary responsibility to various entities. These include, for example, a 3(21) Named Fiduciary to make discretionary decisions and oversee the plan, a 3(16) Plan Administrator and a non- fiduciary third party administrator for the administrative side of the plan, and a 403(a) Trustee or a 3(38) Investment Manager for the investment side of the plan. It's all right there in ERISA, what you're allowed to do and the way to do it.

ERISA really is an exquisite pension law, isn't it?

It really is but only if people are paying attention! And that, I think, is what your last question was getting at. The problem, though, is that through the years, companies sort of lost sight of the fact that they have available to them all these ways of mitigating their risk and at the same time ensuring that their plans are governed by best practices for the benefit of plan participants and their beneficiaries. A good example is Enron. Apart from the outright fraud that resulted in many people losing their jobs and their retirement benefits, what was glaringly apparent was the non-existence of prudent practices governing Enron's retirement plans that if utilized could have benefitted both the board and plan participants. I've paid particular attention to this because over the years my law practice has evolved into one specializing in retirement plan governance and best practices structures governing retirement plans.

Do you think that companies are starting to see the light here?

I think in general they're beginning to wake up because without best practices, they now realize that there's a higher probability that they'll be exposed to personal liability. Other more increasingly probable dangers are sanctions from the IRS and DOL and the relatively recent flurry of participant litigation in the stock drop cases and fee disclosure cases. So I think that more and more companies are finally seeing that they have to get their act together and set up proper governance structures.

What would such a governance structure look like?

Best practices governance structures can be quite different from plan to plan. However, in a typical governance structure for a 401(k) plan, the board of directors would appoint a plan committee as the “Named Fiduciary” under ERISA responsible for plan investments and administration. This limits the board’s liability to a residual monitoring responsibility to make sure that the members of the plan committee are prudently exercising their responsibilities under ERISA. Best practice is to have this monitoring responsibility performed by a committee of the board (such as a benefits committee, audit committee or compensation committee) comprised of individuals who are knowledgeable about the standards required by ERISA and are therefore able to prudently monitor the compliance of the 401(k) plan committee. In turn, the members of the plan committee could appoint appropriate independent fiduciaries if they felt that they weren’t knowledgeable enough about certain aspects of the plan. Or, if the plan committee chose to, it could appoint the 3(21) Named Fiduciary to help them either on the administrative side of the plan or the investment side, or both. On the investment side, for example, the 3(21) Named Fiduciary would have the responsibility of monitoring any 3(38) Investment Managers. On the administration side, you’d have the 3(16) Plan Administrator and the third party administrator to provide best practice governance, giving you monitoring at every level.

Aren’t many companies, even large ones, woefully deficient on the operational and administration side of their retirement plans?

Yes, that’s true. Companies are typically compliant on the investment side but in many cases neglect the oversight required to properly monitor the administration of their plans. For example, when we perform Fiduciary Audit Operational Compliance Reviews for very large defined benefit or defined contribution plans, we rarely find an administration manual. And even if there is, it’s really not an administration manual, it’s not even a good summary plan description booklet; it’s just general boiler plate that only reflects the TPA’s administration of the plan based on their computer systems and not based on the terms of the plan document. So how can anybody monitor a plan’s administration if there’s really nothing describing adequately what to monitor? So you need to start with a proper administration manual which not only reflects plan terms but also incorporates internal control procedures between the employer and TPA to assure that correct information is provided to the TPA.

This is critically important to comply with IRS requirements and avoid the imposition of monetary sanctions on the employer plan sponsor in the event of an IRS audit. Establishing a self-auditing internal control structure is also important to comply with the new accounting rule SAS 115 [Statement on Auditing Standards (SAS) No. 115; Communicating Internal Control-Related Matters Identified in an Audit] which requires plan auditors to make sure that robust internal controls exist with respect to operational compliance with the plan document and all applicable legal requirements. In addition, you have to make sure that the plan document, the summary plan description and the administration manual are consistent with each other. But many companies don't do these things and only wake up when hit with an IRS or DOL audit or participant litigation.

You mentioned that you're now doing some work in the United Kingdom.

I've been representing English clients and U.S. clients operating in the U.K. for almost 30 years. The last five or ten years I've been working more with financial institutions and the U.K. government, specifically the Pension Regulator and Pension Protection Fund, informally advising them on governance and best practices. My law firm has an office in the Netherlands which passed a pension governance law in 2007 that's modeled after ERISA. So what I do in the US, I also do in the U.K. and the Netherlands, and I'm now working with the European Union on the same issues as well. I'm having a great time and enjoying every minute of it. The biggest issue in the U.K., Netherlands and EU is the flight from defined benefit to defined contribution plans and the concerns of regulators about the absence of governance when an employer contracts out their DC plan to an insurance company. The best model for achieving governance in such a situation is a defined contribution multiple employer plan run by a board of independent trustees who are experts in plan investment and administration, including the establishment of best practices governance procedures. So what some say is the best model for a defined contribution plan in the U.S. is now being copied in Europe, and I'm helping the Europeans on that.

Whenever you eventually retire, what would you like your legacy to be?

Well, I'm not sure that I'll ever retire; I really love what I do. But whether or not I ever retire, I guess that I'd like my legacy to be that I tried to provide good governance practices for retirement plans all over the world. I should note that I just experienced the great joy of seeing my son admitted to the bar. He also shares my ideals for honesty and integrity in corporate and retirement plan governance. My ultimate hope and legacy is that he and other young lawyers like him will continue to make sure that ERISA and its important fiduciary requirements are upheld and preserved so as to protect the retirement benefits of future generations.

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