McGriff EMPLOYEE BENEFIT SOLUTIONS

COMPLIANCE Q&A

# Accidental MEWA

**McGriff Employee Benefits Compliance Team**
*National Specialty Practices*

**Question:** Our company (Company A) is a closely owned family business and there is a related company (Company B) that has somewhat similar ownership. Company A is owned by four brothers, W, X, Y and Z, and each owns 25% of the common stock. Company B is owned by the same four brothers (10% ownership each) and their two cousins U and V each own 30%. We always assumed that with this common family ownership we could cover the employees of both Company A and Company B under Company's A's self-insured medical plan. Are there any compliance issues with doing so?

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**Summary:**

While we would need more information on the relationship between the companies, covering Company B's employees under Company A's self-insured medical plan would appear to create a multiple-employer welfare arrangement (MEWA). The Employee Retirement Income Security Act (ERISA) defines a MEWA as: "an employee welfare benefit plan...which is established or maintained for the purpose of offering or providing [welfare benefits] to the employees of ***two or more employers*** (including one or more self-employed individuals), or to their beneficiaries."[1]

When looking at whether there are "two or more employers," ERISA applies controlled group/common control standards from the Internal Revenue Code (Code).[2] If two employers are under common control or a controlled group, they will be considered a single employer and sponsoring the same plan for group medical benefits would not be a MEWA.

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Here, however, it does not appear that the common ownership is sufficient to establish a controlled group or common control under the Code.

A self-insured MEWA, unlike a single-employer self-insured plan, is subject to state insurance regulation.[3] Many states impose a host of requirements on self-insured MEWAs, including reserves, bonding, reporting, etc. States vary as to the regulation of self-insured MEWAs; for example, in California there is an outright prohibition of self-insured MEWAs unless the MEWAs applied for certificates of compliance on or before Nov. 30, 1995.[4] As another example, operating a self-insured MEWA without the proper registration, reserves, or reporting in North Carolina is a felony.[5]

There is often confusion over the ownership threshold for MEWA status, with some believing that 25 percent or more common ownership is sufficient to establish a single-employer plan. While 25 percent or more common ownership may exempt the MEWA from certain filing requirements,[6] generally there must be common control or controlled group status as defined under the Code to escape the application of state law and 25 percent (or even 50 percent) is not sufficient.

In addition to family businesses, “accidental” or "inadvertent" MEWAs can arise in a number of instances. MEWAs can arise from a business owner's succession or estate planning, from mergers and acquisitions, or from covering non-employee members of a board of directors or independent contractors under a group medical plan. Employers should discuss with their legal counsel any risks that may arise when two or more employers who are not under common control or in a controlled group sponsor a single welfare plan.

***Importantly, intent is not a requirement to create a MEWA. If there is insufficient common ownership of companies participating in a single group health plan, a MEWA can be created totally by accident.***

**Detail:**

*Background*

Under ERISA, a MEWA is "an employee welfare benefit plan, or any other arrangement...which is established or maintained for the purpose of offering or providing ...[welfare plan benefits] to the employees of two or more employers (including one or more self-employed individuals), or to their beneficiaries."[7] Excluded from the definition of a MEWA is a plan that is established or maintained under bona fide collective bargaining agreement, by a rural electric cooperative, or by a rural telephone cooperative association.[8]

Unlike single-employer self-insured plans that can rely on ERISA's preemption provisions as to state law, MEWAs are subject to state regulation.[9]

The MEWA provisions were enacted, at least in the view of the Department of Labor (DOL), because of disreputable promoters marketing MEWAs to small employers as an alternative to state-regulated group medical insurance. The marketers would assert that, because of ERISA's preemption provisions, these plans were not subject to state insurance, reserve, contribution, and other requirements. In the early days

of MEWAs, many of these plans failed, leaving employees with unpaid claims and employers without coverage for their employees.[10]

Prior to 1983, state attempts to subject MEWAs to regulation were met with claims of ERISA preemption of state law. Congress recognized there was abuse and ERISA was amended in 1983 to allow states to establish, apply, and enforce state insurance laws with respect to MEWAs.[11]

Unfortunately, as with many areas where there is perceived abuse, non-abusive arrangements can be swept in as well. The following are some MEWA "traps" that we have seen:

- Related companies offer the same benefit plan to their employees, but the companies are not in the same controlled group/common control as appears to be the case in this Q&A.
- Joint ventures where two unrelated companies join together to form a third entity for certain projects and want the joint venture to participate in one of the company's benefit plans.
- A father who has 100 percent ownership in a construction company and 100 percent ownership in a trucking company all on the same benefit plans. As part of his estate plan, he gifts 60 percent ownership in the trucking company to his adult daughter and 60 percent of his construction company to his adult son. He has now likely created a MEWA.
- MEWAs can also be inadvertently created in mergers and acquisitions. For example, a buyer may acquire a division or subsidiary from a seller where that seller maintains a single group health plan for all of its divisions/subsidiaries. The buyer takes the employees associated with that division or subsidiary. The buyer, however, wants some "breathing room" before it establishes its own plans and requests that its newly acquired employees stay on the plan of the seller for a brief period of time. The seller is arguably operating a MEWA for the period of time the seller maintains a plan that includes its remaining employees and the employees who now work for the buyer.
- Finally, allowing non-employee directors or independent contractors on a plan can arguably create a MEWA. Note that ERISA's definition of a MEWA states the requirement of two or more employers can include "one or more self-employed individuals.[12]" Non-employee members of a board of directors are often considered self-employed.

Employers should consult legal counsel with regard to the arrangements discussed above. Counsel may differ on what type of risk each arrangement raises, especially in light of an exemption from certain federal reporting requirements, discussed below.

*Common Control/Controlled Group*

As mentioned, ***if two employers are in a controlled group or common control, then they can sponsor the same benefit plans without creating a MEWA.*** Under ERISA's MEWA definition, whether an entity is determined to be under common control is to be determined under regulations issued by the DOL, applying principles similar to those applied in determining whether there is "common control" under the Code, except that common control shall not be based on an interest of ***less than 25 percent.***[13]

Unfortunately, the DOL has never issued regulations lowering the threshold for common control to 25 percent. Without these regulations, we are left with the Code's definition of common control which, among other things, requires 80 percent common ownership. (For MEWAs, the cross-reference to the Code is actually accomplished through a cross-reference to another section of ERISA which then cross-references the definitions of controlled group and common control contained in Sections 414(b) and 414(c) of the Code).[14] Employers may very well be familiar with the rules under Code Sections 414(b) and 414(c) since they are the same rules for determining controlled group/ common control status for qualified retirement plans.

This issue is addressed in a DOL publication, Multiple Employer Welfare Arrangements under the Employee Retirement Income Security Act (ERISA): A Guide to Federal and State Regulation (MEWA Guide). The MEWA Guide specifically notes the Code's requirement of 80 percent or more common ownership to create common control.[15] The regulations issued under Section 414(c) of the Code, see 26 CFR 1.414(c)-2, provide that "common control" generally means, (i) in the case of a parent-subsidiary group, the entities are connected through at least an 80 percent ownership interest, or (ii) in the case of a brother-sister group: (a) five or fewer persons together own a greater than 50 percent interest in each entity, taking into account the ownership of each person only to the extent such ownership is identical with respect to each organization. Employers may very well be familiar with the rules under Code Sections 414(b) and 414(c) since they are the same rules for determining controlled group/common control status for qualified retirement plans.

Applying the brother–sister common control test to the facts in this Question, neither the 80% nor the 50% requirements are met as the below chart illustrates. A shareholder can be included in the ownership calculation only if he/she has some ownership interest in both companies. Here, U and V cannot be considered because they own 0% of Company A. Looking at W, X, Y and Z, they own 100% of Company A but only 40% of Company B, so the 80% test is not met. Likewise, they only own 40% of both companies when considering identical ownership, so the 50% test is not met. Accordingly, Company A and Company B are not in the same controlled group.

| Owner | Company A | Company B | Identical Ownership |
|---|---|---|---|
| U | 0% | 30% | 0% |
| V | 0% | 30% | 0% |
| **W** | **25%** | **10%** | **10%** |
| **X** | **25%** | **10%** | **10%** |
| **Y** | **25%** | **10%** | **10%** |
| **Z** | **25%** | **10%** | **10%** |
| **Total owned by the same 5 or fewer shareholders** | 100% | 40% | 40% |

For purposes of a MEWA analysis, an affiliated service group alone would not entitle separate employers to be treated as a single employer and avoid MEWA status. This is so even though for retirement plan purposes, multiple entities will also be considered a single employer if they are an affiliated service group (as is the case for entities considered one employer under the common control and controlled group rules). The DOL made this distinction in an Information Letter in 2004.[16]

***Therefore, for any plan that allows two or more employers to participate, or allows individuals who are not common-law employees or retirees of an employer to participate, legal counsel should be consulted on both the ownership structure of the entities adopting the plan, as well as the applicable MEWA laws of the states where the plan has participants.***

*MEWA Reporting and Other Issues*

***MEWAs, whether self-insured or fully insured, have additional reporting requirements.*** There is a federal registration requirement, as well as an annual reporting requirement on Form M-1.[17] If a MEWA is subject to ERISA and must file a Form M-1, then it also must file a Form 5500 regardless of plan size.[18]

It is with respect to Form M-1 reporting where "inadvertent" MEWAs are given some leeway. This leeway, however, does not carry over to a state's ability to regulate the self-insured MEWA as discussed above. A Form M-1 will not be required when one of the following is true:

- There is a common control interest of at least 25 percent.
  - In this Q&A, there would be no M-1 filing requirement because there is 40% common ownership in Companies A and B.
- There is a change in control of businesses (such as a merger or acquisition) that occurs for a purpose other than avoiding Form M-1 filing and is temporary in nature. "Temporary" means the MEWA does not extend beyond the end of the plan year following the plan year in which the change in control occurs.

- The MEWA provides coverage to persons (excluding spouses and dependents) who are not employees or former employees of the plan sponsor, such as non-employee members of the board of directors or independent contractors, and the number of such persons who are not employees or former employees does not exceed one percent of the total number of employees or former employees covered under the arrangement.[19]

***Also, if there are employee/participant contributions to a MEWA, there is often a requirement for a formal trust document unless the MEWA is fully insured and contributions by each employer are sent directly to the insurer.*** This is because the arrangement would fall outside of DOL's non-enforcement policy with respect to trusts contained in Technical Release 92-01 (TR 92-01).[20] A full discussion of TR 92-01 is beyond the scope of this Q&A but the existence of a trust also requires audited financial statements to accompany the Form 5500 if there are over 100 participants in the MEWA at the beginning of the plan year.[21]

## Conclusion:

Self-insured MEWAs can be subject to state laws, which vary. Many states, however, strictly regulate self-insured MEWAs and operating an unlicensed self-insured MEWA can subject the plan sponsor to harsh civil and criminal penalties, depending on the state. Because of this potential liability, counsel should always be consulted when the issue of a possible MEWA arises. MEWAs also can create additional federal filing and reporting requirements. This Q&A is not an exhaustive discussion of the compliance issues facing MEWAs. There can also be issues with fully insured MEWAs, as well as issues with whether the MEWA itself constitutes a single ERISA-covered plan (which would allow it to file a single Form 5500, among other things) or whether each employer participating in the MEWA is deemed to have its own plan for purposes of ERISA (meaning each employer's plan must separately satisfy its ERISA obligations, including, for example, to file a Form 5500). The MEWA Guide mentioned above is a valuable initial resource for MEWA issues.

**References**


1 - ERISA §3(40)(A)(emphasis added).

2 - ERISA §3(40)(B).

3 - ERISA §514(b)(6)(A)(ii).

4 - California Code, Insurance Code – INS §742.23.

5 - N.C. Gen. Stat. §58-49-35 (Any MEWA operating in North Carolina is an unauthorized insurer) and N.C. Gen. Stat. §58-33-95 (Class H felony to know or should have known that insurer is an unauthorized insurer).

6 - DOL Reg. §2520.101-2(c)(2)(ii)(A) (groups of businesses with 25% common ownership exempt from Form M-1 filing requirement).

7 - ERISA §3(40)(A).

8 - ERISA §3(40)(A).

9 - ERISA §514(b)(6)(A)(ii).

10 - MEWA Guide, https://www.dol.gov/sites/default/files/ebsa/about-ebsa/our-activities/resource-center/publications/mewa-under-erisa-a-guide-to-federal-and-state-regulation.pdf at p.3.

11 - MEWA Guide at pp.3-4.

12 - ERISA §3(40)(A).

13 - ERISA §3(40)(B)(iii).

14 - See ERISA §3(40)(B)(iii).

15 - MEWA Guide at p.21

16 - DOL Advisory Opinion Letter, https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/information-letters/05-24-2004.

17 - Reporting is required pursuant to ERISA §§ 101(g), 104(a), 505 and 734 and 29 CFR 2520.101-2 and 103-1. See Form M-1 Filing Instructions, https://www.dol.gov/sites/dolgov/files/ebsa/employers-and-advisers/plan-administration-and-compliance/reporting-and-filing/forms/m1-2018.pdf.

18 - 10 Tips For Filing Form M-1 For Association Health Plans And Other MEWAs That Provide Medical Benefits, https://www.dol.gov/sites/dolgov/files/ebsa/employers-and-advisers/plan-administration-and-compliance/reporting-and-filing/forms/m1-filing-tips.pdf.

19 - Form M-1 Filing Instructions at pp.2-3 (instructions follow the sample form) https://www.dol.gov/sites/dolgov/files/ebsa/employers-and-advisers/plan-administration-and-compliance/reporting-and-filing/forms/m1-2018.pdf.

20 - Technical Release 92-01, https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/technical-releases/92-01.

21 - See generally the instructions for Schedules H and I in the 2018 Form 5500 Instructions, https://www.dol.gov/sites/dolgov/files/ebsa/employers-and-advisers/plan-administration-and-compliance/reporting-and-filing/form-5500/2018-instructions.pdf.

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