

Employee Benefits – Do I Really Have to?

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Objectives

- ✓ Provide a high-level overview of the basic compliance considerations surrounding employee benefit plans.
- ✓ De-mystify (a bit) common benefits issues.
- ✓ Provide practical tips to mitigating benefits risk.

ERISA – The Employee Retirement Income Security Act of 1974

- ERISA covers a wide range of employer-provided plans and programs, including:
 - Qualified Retirement Plans (401(k), defined benefit pension, profit sharing, cash balance)
 - Group Health and Welfare Plans (Medical, Dental, Vision, Life, AD&D, LTD)
 - May cover other plans such as Severance, STD, EAP, Dependent Care FSA, Cafeteria Plans
 - Certain “payroll practices” and “Voluntary” benefits not covered
- Important compliance tenets:
 - Reporting Obligations
 - Participant Disclosure Obligations
 - Fiduciary Responsibilities
 - Prohibited Transactions
 - Separate requirements for defined benefit plans and regulation by the PBGC (Pension Benefit Guaranty Corporation)
- ✓ Identify which plans, programs, policies are ERISA-governed

ERISA

The Employee Retirement Income Security Act of 1974

Reporting

Annual Report – Form 5500s

Retirement Plans with over 100 participants require an external audit

“Top Hat” filings for certain deferred compensation plans

Plan documents are not filed with the DOL but will be requested on audit

Documentation/Disclosure

Formal/Written Plan Document

Trust Agreement for certain plans with plan assets

Summary Plan Description (SPD) and Summary of Material Modifications (SMM)

Summary Annual Report (SAR)

Summary of Benefits Coverage (SBC) (health plans)

COBRA Notices (health plans)

DOL provides detailed rules regarding content, timing, and format (electronic or paper) for each disclosure

Fiduciary Responsibilities

ERISA requires plan fiduciaries to act:

- “With the care, skill, prudence and diligence that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims” (Prudence)
- For the exclusive benefit of Participants and Beneficiaries (Exclusive Benefit)
- Solely in the interest of participants and beneficiaries (Loyalty)
- Maintain a Fidelity Bond

ERISA – The Employee Retirement Income Security Act of 1974

- Enforced by the U.S. Department of Labor
 - DOL actively audits ERISA compliance through random and targeted audits
 - Current priorities for the DOL include:
 - Health plan compliance with the Mental Health Parity and Addiction Equity Act
 - Cybersecurity for Retirement Plans
 - Missing Participants
 - Late Contributions
- There are positives to being ERISA-governed!
 - Claimants must exhaust an internal claims and appeals process prior to filing suit
 - A deferential standard of review provided in litigation
 - No right to a jury trial
 - Preemption of state law
- ✓ Understand who does what internally (and externally) to monitor compliance for each ERISA-governed plan. Examine committee and governance structures.

Internal Revenue Code

- The Internal Revenue Code contains its own compliance rules that govern the provision of tax-favored benefits
- The Tax Code overlaps with ERISA and provides rules necessary to maintain “tax-qualification” while ERISA generally covers participant protections
- Code requirements are enforced by the Employee Plans office of Tax-Exempt and Government Entities (TE/GE) division of the IRS through audits and correction programs

Internal Revenue Code Focus

Nondiscrimination

- Generally provides that tax-favored benefits must be provided to non-highly compensated employees on roughly the same basis as highly compensated employees and in some cases measures utilization – i.e. Dependent Care FSA
- Annual testing requirements
- Applies to:
 - Qualified Retirement Plans
 - Self-Insured Medical Plans
 - Pre-tax Cafeteria (Section 125) benefits (including FSAs)
 - Tax-qualified fringe benefits (transportation, qualified tuition, adoption assistance)

Plan Qualification Requirements

Retirement Plan requirements:

- Minimum benefit requirements such as limits on:
 - Eligibility requirements (limited exclusion of PT employees)
 - Vesting schedules
 - Distribution options/requirements (MRD)
 - Statutory limits on maximum benefits (increased with COLA)
- Cafeteria Plans, Health plans and fringe benefits have their own specific design limitations
- ✓ Addressing nondiscrimination and qualification requirements in advance can help avoid more painful fixes later

Provisions Common to the Code and ERISA

- Regulation of Prohibited Transactions
- COBRA Requirements
- Delinquent Contributions/Excise Taxes
- The IRS and DOL can share information for enforcement purposes, but generally speaking reasonable correction steps will satisfy both agencies

Code Section 409A

- Governs deferred compensation arrangements – a legally binding right to compensation that is paid in a subsequent year
- Enacted post-Enron (2004) and far-reaching with the intent to ensure executives don't get preferential treatment rather than being treated as general creditors (as is required with unfunded deferred compensation arrangements)
- Applies to various forms of deferred compensation (including employment agreements, severance agreements, bonus plans). Anything that promises a payment in one year and pays in a later year.
- Generally provides that amounts that are considered deferred compensation must not be subject to acceleration or deferral by the employer or the participant
- ✓ Ensure those responsible for negotiating employment and severance agreements, and drafting bonus and incentive plans are attuned to (or reaching out to someone else) to review for 409A compliance

Benefits Considerations in Corporate Transactions

- Due Diligence on Seller's Plans
 - High Risk Items
 - Defined Benefit Pension Obligations (underfunding)
 - Multiemployer Plan Withdrawal Liabilities
 - ACA Compliance/Penalty Exposure
- Representations and Warranties – Parties to the deal have options as to how to handle plans, including terminating seller's plans prior to close to limit liability
- Common Post-Close Benefits Integration Issues
 - Separate plans, imputing service credit, plan adoption, plan mergers, rollovers, treatment of outstanding plan loans
 - Where separate benefits continue to exist, Controlled Group nondiscrimination testing, harmonization, administration, fiduciary responsibilities
- ✓ Don't forget to consider benefits plans compliance in advance of closing where possible and involve benefits counsel (in addition to deal counsel)

Benefits Considerations in Separation Agreements

- Separation Agreements should be vetted/reviewed for benefits issues – including:
 - Post-termination health coverage
 - COBRA Subsidies
 - Discrimination concerns under 105(h) of the Code for self-funded medical plans
 - Special Issues for those who are Medicare Eligible
 - Marketplace enrollment windows following expiration of subsidies
 - Tax treatment of other benefits such as outplacement, repayment of loans, treatment of other fringe/perks
 - 409A Compliance
 - Ensure any new payment commitments are either:
 - Exempt – qualifies as (1) a Short-Term Deferral (paid no later than 2-1/2 months after the year in which the right to the payment is vested) or (2) Separation Pay (payment is no more than 2x the lesser of base salary or the compensation limit under the Code and is paid no later than 2 years following the year of termination).
 - Or compliant – sets clear time and form of payment, no ability to accelerate or defer, if publicly traded and individual is a “Specified Employee”, payment is delayed for 6 months following separation.

Operational Compliance

- Often efforts are focused on document compliance, but just as important if not more, is operational compliance.
- Follow the terms of the plan – Failure to do so can present tax-qualification and fiduciary breach risk
- Operation and administration implicates a variety of parties and requires coordination:
 - HR
 - Benefits
 - Payroll
 - Third Party Administrators/Recordkeepers
 - Insurers
 - Actuaries/Consultants
 - Legal

✓ Understand who is responsible for what and make sure efforts are coordinated

Self Correction of Failures

- Errors are common even in the best administered plans. Various regulatory agencies do not have the bandwidth to monitor and enforce every failure and have promulgated voluntary correction programs to incentivize plan sponsors to monitor compliance, identify failures and take proactive steps to correct.
- Utilization of voluntary compliance programs generally does not lead to wider scale audits
- Correction programs can be raised when failures are detected on audits conducted in connection with 5500 reporting requirements
- Fees for correction are generally reasonable and set to incentivize self-correction
- ✓ Monitor on-going compliance and respond to “issues” quickly with the goal of self-correcting in accordance with guidance
- ✓ How an issue arises (internal/external audit, participant claim) can dictate the correction

Internal Revenue Code

IRS – Employee Plans Compliance Resolution System (EPCRS)

- Voluntary programs with (VCP) and without (SCP) IRS approval to correct various, common errors in qualified retirement plans
- Goal is generally to put the plan and the participants in the place they would have been in had the failure not occurred and keep assets in the plan
- Common failures include misapplication of plan terms (definition of “compensation”, excess contributions, overpayments, underpayments)

DOL

- Correcting late 5500 filings
- Voluntary Fiduciary Correction Program (VFCP)
 - Delinquent Contributions
 - Prohibited Transactions

IRS – 409A

- The IRS has issued guidance to correct documentation and operational failures to comply with 409A
- Tax consequences and correction methods vary based on how early the failure is identified and corrected
- More favorable tax treatment than if detected on audit
- 409A tax consequences rest largely on the participant and not the employer

Private Litigation/Claims

- Individual Claims

- ERISA requires an individual to follow internal plan claims and appeals process before filing litigation
- Private rights of action generally take the form of either a claim for a denial of benefits (where relief is limited to the benefit under the plan) or a breach of fiduciary duty claim (which can include equitable relief)

- Class Actions

- Over the last 10 years, there has been an proliferation of class actions under ERISA – primarily focusing on 401(k) plan fees and investments.
 - Underscores importance of plan governance and ongoing monitoring of plan services, investments and providers.
 - Fiduciary Liability Coverage
 - Participant Communications, including clear fee disclosures.
- ✓ Make sure fiduciary liability coverage is reviewed and best practices are implemented and monitored to mitigate litigation risk

Key Takeaways

- ✓ Put benefits on the list of items to consider up front in M&A transactions, separation agreements, RIFs
- ✓ Review internal governance and fiduciary structures around benefit plans
- ✓ Stay tuned, especially now. COVID-related and Biden Administration priorities will lead to additional legislation and regulation impacting benefit plan compliance
- ✓ CARES Act, ARPA, SECURE Act, SECURE 2.0, Health Plan Mandates: Price Transparency, No Surprises Act, Mental Health Parity, and ACA enforcement and expansion to name a few
- ✓ Other tax legislation, Medicare, and ACA Marketplace changes will directly impact benefit plans as well as a proliferation of state law directives related to benefits

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Thank **you.**