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EMPLOYEE BENEFITS AND EXECUTIVE COMPENSATION

EMPLOYEE BENEFITS YEAR-END CHECKLIST

2018 EMPLOYEE BENEFITS YEAR IN REVIEW—PLANNING AHEAD FOR 2019

With the end of the calendar year drawing near, this is a good time for employers to conduct a year-end review to make sure their benefit plans are up-to-date and operating in compliance with the law. In addition, the end of the year brings a number of important deadlines. To assist you with your year-end projects, this newsletter provides a summary of some important dates and new developments.

Important Reminders for 2018

- Some (but not all) of the benefit limits will increase for 2019, so your payroll and recordkeeping systems will need to be updated. A table setting forth the 2018 and 2019 IRS limits appears at the end of this newsletter.
- If you have participant-directed investments and utilize a "Qualified Default Investment Alternative" ("QDIA") for "default" investments, you should provide your default investment informational notice by December 1, 2018 if you have a calendar year plan year. Your plan recordkeeper generally will assist you in preparing the notice and coordinating its distribution.
- If you have a "safe harbor" 401(k) or 403(b) plan or want to adopt a safe harbor structure for 2019, you must provide your annual notice by December 1, 2018 if you have a calendar year plan year. This applies regardless of whether you are using a traditional safe harbor or an automatic enrollment safe harbor. Make sure the notice includes a warning that the employer retains the right to reduce or eliminate safe harbor contributions, in order to preserve this ability for you if you need it.
- If you have an automatic enrollment 401(k) or 403(b) plan, regardless of whether it is a "safe harbor" plan, you must provide your automatic enrollment annual notice by December 1, 2018 if you have a calendar year plan year.
- Participant-directed defined contribution plans must provide annual notices regarding plan expenses and investments. Plans should be sure they have met that obligation; the deadline will vary depending on the timing the plan has established. Disclosures must be provided no more than 14 months after the previous year's fee disclosure.
- If you want to make any amendments to your qualified retirement plan, you may need to adopt them before the end of the current plan year. Generally, an amendment to a qualified retirement plan that takes effect during a plan year must be adopted before the end of the plan year, unless Congress or the IRS has granted an extension.
    - For plans that took advantage of special IRS rules relating to hardship withdrawals or loans associated with economic losses caused by Hurricanes Harvey, Irma, Maria and/or the California

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wildfires in 2017, plan amendments may be required before the end of the 2018 plan year. Amendments relating to the special distribution and loan rules in the Disaster Tax Relief and Airport and Airway Extension Act of 2017 and Bipartisan Budget Act of 2018 are due by the end of the 2019 plan year.
  - Some amendments must be in place before the desired effective date (for example, if you are changing your contribution structure, an advance amendment may be required).
  - Changing a 401(k) or 403(b) plan to or from a "safe harbor" structure usually requires an amendment in advance of the start of the plan year, and certain changes to those plans cannot be made after the start of the year. If you have one of these plans, it is important to plan ahead.
  - Adding or changing an automatic enrollment feature to a 401(k) or 403(b) plan may also require an amendment before the start of the plan year.
- Benefit statements
  - Remember that you must provide benefit statements for your participant-directed plans within 45 days of the end of the quarter, and for non-participant-directed defined contribution plans by the filing date for Form 5500 for the plan year.
  - If you sponsor a defined benefit plan, you must either provide employed participants with an annual notice of the availability of a benefit statement on request, or with an actual benefit statement once every three years. (Bear in mind that the statute does not exempt frozen plans from these requirements.) Defined benefit plans sponsored by employers with intranet sites may also be required to make certain information available on the intranet site within 90 days of filing Form 5500.
  - If you meet the benefit statement requirement by providing continual online access to statement information, remember to provide participants and beneficiaries with an annual notice explaining how they can access their benefit statement information and informing them of their right to a paper copy, free of charge, upon request.
- Make sure that you or your insurer have provided all notices required under your group health plan this year, which may include the Women's Health and Cancer Rights Act notice, the Children's Health Insurance Plan notice, notice of availability of the Health Insurance Portability and Accountability Act (HIPAA) privacy notice, and/or the Medicare Part D notice, and that you or your insurer provide required Summary of Benefits and Coverage documents during your open enrollment period.
- Most retirement plan participants are required to receive annual "required minimum distributions" after turning age 70½ and terminating employment with the plan sponsor (or after turning age 70½, in the case of a more-than-5% owner). Time limits also apply to payment to beneficiaries of deceased participants. Each year's payment must be made by December 31st with the exception of a participant's first required minimum distribution (due April 1st of the following year). Make sure that your plan has arranged to make all required payments, and has up-to-date addresses for affected participants and beneficiaries.
  - As the population ages, more and more plan participants are affected by these deadlines. The IRS and the Department of Labor have increased the resources dedicated to enforcing these rules, and

require plans to indicate on Form 5500 whether they failed to make required payments (see "Continued Regulatory Focus on Retirement Plan Payment Deadlines" below).

- If you expect to have assets remaining in your defined contribution plan's forfeiture account at the end of the year, you should review your options and obligations under the plan document to determine whether you can (and whether you must) make arrangements to use up your forfeiture account this year. The IRS has emphasized that plans generally should not be carrying forfeiture balances over from year to year. As a corollary of this analysis, make sure that your recordkeeper is processing forfeitures in a timely fashion when former employees take distributions or complete five breaks in service, so that the forfeited money can be put to proper use.
  - In this regard, it is worth noting that in 2017, the IRS changed its position and began allowing forfeitures to be used to fund safe harbor contributions to 401(k) and 403(b) plans as well as certain other types of contributions for which forfeiture funding previously was disallowed. Regulations to this effect were finalized in 2018. Employers that want to take advantage of this new rule should adopt any requisite amendments by the applicable deadline.

A Look Ahead at 2019

There are some important action items to bear in mind as 2019 gets underway:

- A new pension mortality table took effect January 1, 2018 for purposes of calculating defined benefit plan lump sum distributions. The new mortality guidelines also applied for purposes of calculating funding obligations for plan years beginning on or after January 1, 2018, but the IRS offered liberal grounds for employers to obtain an extension of the deadline for this purpose. Businesses that claimed extensions on the grounds of hardship will need to begin using the new tables for funding purposes for the 2019 plan year. The IRS anticipates issuing new tables annually roughly twelve months in advance of each new table's scheduled effective date, and issued the tables for 2019 at the end of 2017, to give employers plenty of time to plan.
- Under the Patient Protection and Affordable Care Act, larger employers can face a "shared responsibility" (a.k.a. "pay or play") penalty if they fail to offer full-time employees affordable medical coverage. Larger employers are also subject to an information reporting requirement that requires them to track employees' hours of service as well as information about their offers of coverage to their full-time employees during the year. The IRS has released draft instructions and forms for the 2018 filing, which are available here: https://www.irs.gov/pub/irs-dft/i109495c--dft.pdf. For the 2018 filing, copies of the 1095-Cs are due to individuals by January 31, 2019, and copies of the 1094-Cs and 1095-C forms are due to the IRS by February 28, 2019, or April 2, 2019, if filing electronically.
- If required, an employer with a self-insured medical plan may need to make a second request for a taxpayer identification number ("TIN") (i.e., a Social Security Number) for employees who have not provided a requested TIN. As noted above, under the Affordable Care Act, larger employers are subject to information reporting requirements regarding employee full-time status and offers of coverage. The IRS Forms used for this purpose require that TINs be included on the Form. Employers with self-insured medical plans are responsible for collecting (or attempting to collect) TINs for

employees and their family members who enroll in the employer's medical coverage. The IRS proposed regulations that provide a waiver from penalties if the employer is unable to obtain necessary TINs but has taken "reasonable steps" to collect such TINs, which consists of making a solicitation within the following timeframes:

- upon enrollment,
- within 75 days after the date of the initial solicitation, and
- by December 31 of the year following the year in which the individual applied for coverage or added an individual to existing coverage.

If an employee does not provide a TIN for a covered spouse or dependent, the employer may use that individual's date of birth on Form 1095-C in lieu of a TIN.

- The Health Information Technology for Economic and Clinical Health Act (the "HITECH Act") requires group health plans to notify the Department of Health and Human Services ("HHS") of all breaches of unsecured protected health information. You must notify HHS within 60 days of discovering a breach affecting 500 or more individuals. For breaches involving fewer than 500 individuals, HITECH requires a group health plan to keep a log or other documentation of such breaches that occur within a calendar year and to notify HHS of such breaches within 60 days of the close of the calendar year. This means that you must notify HHS of all breaches affecting fewer than 500 individuals that occurred in 2018 by no later than March 1, 2019. Notifications must be submitted online at http://www.hhs.gov/ocr/privacy/hipaa/administrative/breachnotificationrule/brinstruction.html.
- Medicare Part D online disclosure to the Centers for Medicare & Medicaid Services ("CMS") for group health plans offering prescription drug coverage to individuals eligible for Medicare Part D is due by March 1, 2019.

Important Developments in 2018

A number of developments occurred in 2018 that affect employee benefit plans, including a court decision invalidating the Department of Labor's regulations seeking to expand the definition of "fiduciary" under ERISA, a continuation of robust litigation activity focused on defined contribution plan investment performance and cost, new disability claims regulations taking effect and changes to the rules for qualified plan hardship distributions. This segment of the newsletter summarizes the items we have found to be most relevant to our clients.

Impact of Tax Cuts and Jobs Act and Bipartisan Budget Act

Changes to Hardship Withdrawal Rules

Under the Bipartisan Budget Act, changes to rules governing hardship withdrawals from 401(k) plans will take effect for plan years beginning after December 31, 2018. Most and potentially all of these changes are expected to apply to 403(b) plans as well. Specifically:

- More types of contributions will be available for hardship withdrawal. At present, plans cannot allow hardship withdrawals from post-1988 earnings on elective deferrals, post-1988 qualified nonelective contributions ("QNECs") or post-1988 qualified matching contributions ("QMACs"), including QNECs and QMACs used as "safe harbor" contributions for plans exempt from ADP and/or ACP testing. The new legislation removes this prohibition, although some technical defects call into question whether safe harbor contributions under a Qualified Automatic Contribution Arrangement will qualify for hardship withdrawals.

- Employees who take a hardship withdrawal will no longer be required to suspend future contributions to the plan and most other employer plans for six months.
- Employees will no longer be required to obtain plan loans (if available) prior to taking a hardship withdrawal.

The IRS has yet to issue guidance regarding these changes. We anticipate, however, that employers will be able to choose whether or not to implement these changes or retain the more restrictive rules in effect under prior law. The one exception may be safe harbor plans, which we anticipate will be required to eliminate the six-month suspension on elective deferrals. The same may apply to 403(b) plans due to the "universal availability" rule applicable to those plans which normally require most employees not within a handful of specified excludable categories to be able to make deferrals. (Depending on the details of their design, plans with "eligible automatic contribution arrangements" also may be required to eliminate the suspension rule.) More information about these changes and the considerations employers may want to take into account before deciding whether to adopt or reject these changes is available in our newsletter at https://www.hselaw.com/news-and-information/legalcurrents/1444-retirement-plan-hardship-withdrawals-new-rules-for-2019.

Measures to Prevent Loan Defaults

The Tax Cuts and Jobs Act allows a participant who has an outstanding plan loan at the time of termination of employment or termination of the lending plan to roll the outstanding loan amount over by the deadline for the participant's tax return for the year in which the loan amount is treated as a plan distribution. Prior to this change, participants only had 60 days to complete a rollover.

It is important to understand that completing such a rollover would require rolling over the *amount of the outstanding loan*, rather than the loan obligation. Accordingly, participants seeking to take advantage of this new right will need to find the requisite cash from another source. This is different from the situation of participants who are permitted to roll over the actual loan note itself and continue repaying the note to a new employer's plan. However, most plans only make loan note rollovers available to participants affected by a business divestiture. If a participant's employment and/or plan terminates in other circumstances and the participant is not allowed to continue making repayments to the lending plan, the extended rollover period will give the participant more opportunity to find the necessary financing to fund a rollover and thereby to prevent the adverse tax consequences of a loan default.

Other Retirement Provisions

The Bipartisan Budget Act addresses some other retirement concerns as well. It includes relief from certain tax consequences for qualifying distributions and enhanced rollover opportunities for individuals tapping retirement funds to cover costs associated with the 2017 California wildfires. It establishes a Congressional committee to address concerns about multiemployer pension plan funding. Finally, it provides individuals whose retirement savings were seized by an improper federal tax levy to avoid taxation by rolling the affected funds (plus interest) back to a plan or IRA by the tax filing deadline for the year in which the wrongfully seized funds were refunded.

Indirect Impact

In addition to the handful of provisions directly related to retirement, these two statutes include other provisions that indirectly affect retirement plans. For example:

- Some companies responded to the lower corporate tax rate created by the Tax Cuts and Jobs Act by offering one-time special retirement contributions, or by making longer-term enhancements to retirement contribution rates.
- Changes to the tax treatment of various types of compensation and employment-related benefits may alter the amount of compensation included in retirement plan formulas. The change with the greatest impact on retirement plans probably is the repeal of the income exclusion for certain moving expense reimbursements effective 2018 through 2025. Moving expense reimbursements will be includible in gross income during this period. You should review your retirement plan's definition of compensation to ensure that it provides for the desired treatment of moving expenses and other items of compensation and that your payroll administration follows the definition of compensation in your plan document.
- Changes to the rules for qualifying a loss as a "casualty loss" for purposes of federal income tax deductions may limit a participant's ability to take a hardship withdrawal, since the need to cover expenses associated with a casualty loss is an IRS-approved hardship trigger. The more restrictive definition of "casualty loss" therefore is likely to reduce access to hardship withdrawals.
- Changes to the rules on "unrelated business taxable income" may affect retirement plans with investments that generate this type of income. "UBTI" issues most commonly arise in connection with investments in master limited partnerships, private equity funds not designed to avoid or minimize UBTI, and leveraged investments not structured through a corporation. The IRS has published temporary guidance implementing the new UBTI rules pending issuance of regulations. Plans with investments that generate UBTI should review the economic impact of the new rules and discuss their tax reporting obligations and any desired changes to their portfolios with their advisers. More information is available in our newsletter at https://www.hselaw.com/news-and-information/legalcurrents/1480-irs-issues-ubit-siloing-guidance.
- If an IRA owner converts traditional IRA funds to Roth IRA status, he/she will no longer have the ability to "recharacterize" (i.e., effectively reverse) that conversion prior to the tax return deadline for the year of the conversion.

States Take the Individual Mandate into Their Own Hands

The Tax Cuts and Jobs Act (the "Act"), enacted in December 2017, effectively eliminates the Affordable Care Act's so-called "individual mandate" by reducing the tax-penalty for failing to have health insurance coverage in a year from upwards of $695 (or more, depending on income level) to $0. The provision of the

Act reducing the penalty to $0 takes effect beginning with the 2019 taxable year. By incentivizing all citizens, including healthy individuals, to purchase health insurance, the individual mandate was designed to help stabilize the insurance market. The Congressional Budget Office estimated that the repeal of the individual mandate could result in an additional 3 million individuals without insurance in 2019. In response to the elimination of the penalty and its potential impact on the insurance market, some states have, and others are considering, enacting their own individual mandates as a way to protect consumers and prevent destabilization of the insurance market in their states.

Recently, the States of New Jersey and Vermont and the District of Columbia have passed individual mandates, and Massachusetts had an individual mandate before the Affordable Care Act was enacted. Several other states are currently considering legislation. For some of the states that enacted legislation, the Affordable Care Act's individual mandate was the starting template. For example, the State of New Jersey's tax penalties and reporting requirements generally track the rules under the Affordable Care Act.

With the enactment of state individual mandate laws, employers with employees in multiple states should monitor state law developments, as some of these laws may impose significant reporting, financial, and/or coverage requirements on employers. At this point, it is unclear exactly how employers will be impacted by the new laws in New Jersey, Vermont, and the District of Columbia. Vermont has yet to issue any guidance on its mandate, and it appears that New Jersey and the District of Columbia will require employers sponsoring group health plans to submit an annual return. If a state imposes a coverage or reporting requirement on an ERISA-covered employer, the law would arguably be preempted by ERISA, but with different courts reaching different conclusions on ERISA preemption, it is difficult to predict whether all such requirements will be preempted. We will continue to monitor state legislative efforts as well as any court cases regarding preemption.

Supreme Court News

Epic Systems Arbitration Ruling

In *Epic Systems v. Lewis*, the Supreme Court rejected the premise that mandatory arbitration clauses with class action waivers were automatically impermissible in the employment-dispute context. More information about the case is available at https://www.hselaw.com/news-and-information/legalcurrents/1396-supreme-court-rules-in-favor-of-class-action-waivers-in-arbitration. While the ruling did not address employee benefits claims, it at least removes the concern that benefit plan arbitration clauses with class action waivers were *per se* impermissible under labor relations laws.

Since the Court's decision in *Epic Systems*, lower courts applying the decision in ERISA cases have analyzed the timing of the addition of the relevant arbitration clause to the plan or employment agreement, and whether the claimant was still a plan participant and/or employee at that time. Courts have also reviewed whether there was "consideration" for the addition of a clause (i.e., whether the employee/participant received something of value in exchange for "agreeing" (or being deemed to agree) to the clause). It remains unsettled whether a clause can apply to benefits earned prior to the creation of the clause.

Even if these issues are resolved in the employer's favor in a given case, the clause by its terms must extend to the type of claim at issue. For example, a clause calling for arbitration of claims for benefits may not apply to a claim for a breach of fiduciary duty. Likewise, the clause must bind the proper parties. In *Munro v. University of Southern California*, the court determined that the arbitration clauses at issue applied to the participants, not the plan, and hence could not require arbitration of a claim brought on behalf of the plan. The university has announced that it intends to seek Supreme Court review, and it remains to be seen whether other courts will agree with this result. A case is currently pending in the Second Circuit on the question of whether claims on behalf of the plan can be forced into arbitration, and Schwab is seeking enforcement of a no-class-action arbitration clause in the Ninth Circuit with respect to accusations of inappropriate plan investment in proprietary funds.

Accordingly, while *Epic Systems* has resolved one important issue, plan sponsors, fiduciaries, and ERISA claimants will need to monitor future developments in this area.

Retiree Welfare Benefits

The Supreme Court reversed two Sixth Circuit rulings in favor of retirees seeking to halt cuts to post-retirement benefits in *CNH Industrial N.V. v. Reese and Kelsey-Hayes Co. v. Int'l Union*. The Court's decisions resoundingly rejected the Sixth Circuit's historical tendency to favor union retirees when interpreting collective bargaining agreement provisions about the duration of retiree health and life insurance benefits. The Court instructed the Sixth Circuit to analyze collective bargaining agreements using "ordinary principles of contract law" and to dispense with drawing inferences in favor of the retirees. This decision should make it easier for employers in the Sixth Circuit to win the right to amend or terminate retiree benefits. However, the actual terms of a particular collective bargaining agreement will control the rights of the employees receiving benefits under that agreement, so each case will need to be decided on its own merits.

Wellness Program Developments

Many employers offer incentives to their employees for undergoing medical examinations or completing health risk assessments. Some employers also offer incentives for employees' spouses to participate in such assessments and examinations. A recent federal court decision calls into question the ability to offer such wellness incentives in 2019.

These types of employer wellness programs must comply with the well-settled Health Insurance Portability and Accountability Act (HIPAA) wellness program requirements (if they are offered in connection with a group health plan) and must also comply with the requirements of the Americans with Disabilities Act (ADA) and the Genetic Information Nondiscrimination Act (GINA). An AARP lawsuit against the Equal Employment Opportunity Commission (EEOC) resulted in the invalidation of portions of the EEOC's 2016 ADA and GINA regulations, beginning in 2019. The EEOC is not expected to issue new guidance before then, so employers must go back to the pre-regulation guidance board to assess their wellness plan compliance with ADA and GINA.

ADA

The ADA generally restricts employers from making disability-related inquiries and requiring medical examinations of their employees. There is a limited exception for "voluntary" wellness programs designed to promote health and prevent disease. Through a compliant wellness program, employers may offer an incentive for employees to undergo medical examinations (e.g., biometric screenings) or answer questions about their health status (e.g., a health questionnaire).

Prior to its 2016 regulations, the EEOC offered little guidance on when a wellness program would be considered "voluntary" under the ADA. The most useful guidance was an information letter issued by the EEOC in 2000 stating that a wellness program is voluntary if the employer does not require employees to participate and does not penalize employees who do not participate. Employers were left to guess as to the amount of incentive (if any) that could be provided to encourage participation in such a wellness program. Despite having not issued guidance, the EEOC sued several employers in 2014 on the ground that their wellness incentives were so large as to make the programs involuntary, and thus prohibited, under the ADA.

The 2016 regulations provided relief, specifying that a wellness program would be voluntary under the ADA if the total reward offered did not exceed 30% of the premium for self-only coverage under the employer's group health plan.

GINA

Under GINA, employers generally may not request the genetic information of employees or their family members. EEOC regulations issued in 2008 created a limited exception for employers to request genetic information in connection with a wellness program (provided certain conditions are met), but specifically prohibited the offering of rewards to induce employees to provide genetic information. To complicate matters further, Congress wrote the GINA law to treat medical information regarding an employee's spouse to be the genetic information of the <u>employee</u> (e.g., the fact that a spouse had cancer is considered the <u>employee's</u> genetic information). As a result, prior to the 2016 EEOC GINA regulations, wellness programs that asked employees about their family medical history or asked spouses to undergo an examination or answer questions about the spouse's health conditions (all considered the <u>employee's</u> genetic information) had to (among other requirements) make clear that the incentive would be provided even if the questions weren't answered or the examination was not completed.

The 2016 EEOC GINA regulations created an exception to GINA's prohibition on offering an incentive for a spouse to provide his or her medical information. The regulations allowed employers to offer incentives for a spouse to answer health questions or undergo a medical examination provided the incentive did not exceed 30% of the premium for self-only coverage under the employer's group health plan and certain other conditions were met.

AARP v. EEOC

In 2017, the AARP sued the EEOC on the grounds that the EEOC had not adequately substantiated its rationale for adopting the 30% limit. The court agreed, invalidating, effective January 1, 2019, the sections of the regulations that authorized the 30% incentive limit and allowed an incentive for a spouse to undergo a medical examination or answer medical questions. Until the EEOC issues new regulations, the permissibility of wellness incentives that implicate the ADA or GINA is in a state of limbo.

With 2019 annual enrollment approaching, employers should consider whether it is advisable to offer wellness programs that implicate the ADA or GINA. With the invalidation of the helpful sections of the 2016 EEOC regulations, employers that offer incentives for employees to provide their own medical information (through examination or questions) will need to decide what level of incentive is permissible under the once again undefined "voluntary" standard under the ADA. Under GINA, the ability to offer an incentive for a spouse to undergo a medical examination or answer medical questions will be even more tenuous and will require careful analysis. Many employers may conclude that offering incentives for spousal participation is too burdensome and not worth the risk.

Throughout the AARP lawsuit, the EEOC vigorously defended its position that the 30% limits were "voluntary." Hopefully, that will make it unlikely that the EEOC would bring an enforcement action against an employer that offers wellness incentives that comply with the 30% limit. Of course, there is no guarantee that the EEOC will refrain from enforcement, and under the ADA and GINA, individuals can bring their own lawsuits for violations. Employers should be cognizant of these risks when designing their wellness programs for 2019.

Ongoing Trends in Defined Contribution Plan Litigation

Plaintiffs continue to challenge the investment practices and fee arrangements of defined contribution plans. In 2018, much of the courtroom activity and press coverage has focused on (i) organizations that offered their own proprietary (and allegedly underperforming and overpriced) funds in their retirement plans, and (ii) colleges and non-profit healthcare organizations with decentralized and allegedly excessively expensive 403(b) plans. Institutions offering stable value funds have also faced challenges to the investment strategies and/or compensation strategies of those funds. Finally, plaintiffs continue to face an uphill fight in challenges to plan investment in employer stock, although challenges to specific ESOP transactions have met with some success.

Proprietary Funds

A few plan sponsors facing proprietary-funds challenges have succeeded in having the cases dismissed, such as Wells Fargo and Putnam Investments, but they are in the minority. Others have settled, including Allianz SE ($12 million), TIAA ($5 million) and Deutsche Bank ($21.9 million). More cases are pending.

403(b) Fee Challenges

Likewise, courts have generally declined to dismiss actions against non-profit and educational institutions prior to trial, although the University of Pennsylvania, Northwestern University and Washington University in St. Louis have succeeded in their dismissal efforts (appeals are pending). Employers have had better luck obtaining dismissal of certain specific claims, however, such as challenges to an allegedly excessive number of investment options. Thus, a number of plaintiffs have been allowed to proceed with their cases but seen their list of claims trimmed. New York University prevailed after trial; that decision also has been appealed, and a motion for a new trial is pending based on allegations of a judicial conflict of interest. Many other cases remain pending. Notably, a court recently granted plaintiffs the right to a jury trial in their action against Cornell University, which is unusual in the ERISA context.

Stable Value Cases

A number of prominent financial institutions, such as Principal and Great-West, have prevailed against plaintiffs challenging insurers' rights to set the products' interest rates. The challengers allege that this power results in the insurers controlling their own compensation in violation of ERISA's prohibitions on such control. The interest rate credited to participants in the funds affects the amount of investment earnings above and beyond the fixed interest rate available for retention by the insurer, and plaintiffs therefore assert that insurers can manipulate their gain from the arrangement. Courts have rejected this argument.

Turning to another stable value controversy, courts have also generally been disinclined to second-guess investment strategies, handing a victory to CVS and to Fidelity with respect to challenges that their stable value funds were too conservatively invested.

Stock Drop Claims

Plaintiffs' efforts to hold fiduciaries responsible for losses arising from drops in value of employer stock held in qualified retirement plans continue to meet dead ends in the wake of the Supreme Court's 2014 *Fifth Third Bancorp v. Dudenhoeffer* decision and subsequent ruling in *Amgen, Inc. v Harris*. Following these rulings, courts have held that in order to succeed on these claims, plaintiffs must demonstrate not only that the fiduciaries could permissibly have taken some form of corrective action without violating securities laws, but that a prudent fiduciary "could not have concluded" that the proposed corrective action "would do more harm than good." For example, freezing future stock purchases would prevent additional purchases at inflated prices, but might also cause a market panic that would deflate the value of the stock already held by the plan, and hence would not meet this standard.

Accordingly, recent decisions offer reassurance to fiduciaries whose plans include company stock. That said, litigation risks associated with company stock in the event of a stock drop (or, ironically, a stock price increase from which some or all plan participants were prevented from benefiting due to forced sales or (alleged) concealment of information) remain meaningful. Plan fiduciaries need to be sure they understand the *Dudenhoeffer* standard as it applies to their company's situation, and plan sponsors need to be thoughtful about whether continuing to allow plan fiduciaries to offer company stock as either an active or frozen investment makes sense from the perspective of potential litigation risk and expenses.

In addition, fiduciaries of privately held employee stock ownership plans considering a purchase or sale of company stock should bear in mind that the extent to which *Dudenhoeffer's* protections apply to them remains unsettled. While some courts have followed *Dudenhoeffer* in the private company context, *Dudenhoeffer's* underlying premise (the availability of a price set by an efficient market) does not pertain to private companies. Private companies also are not subject to the public disclosure requirements applicable to public companies, which means fiduciaries may have different options for dealing with a corporate crisis without causing ripple effects. Finally, private companies may offer more opportunity for management conflicts of interest. In the event of a challenge by the Department of Labor or private plaintiffs, liability for settlement or after an unsuccessful defense at trial can range into the multiple millions of dollars.

Robo-Advisers

After unsuccessful attempts to sue several large plan recordkeepers regarding allegedly excessive fee arrangements with popular "robo-adviser" Financial Engines, plaintiffs' attorneys brought suit directly against Financial Engines and Home Depot, sponsor of a plan that offered Financial Engines' services through its recordkeeper. The lawsuit (which also challenges some of the funds offered under the Home Depot plan as imprudent choices due to underperformance), asserts that fee "kickbacks" from Financial Engines to the recordkeeper constituted "prohibited transactions" that violated Section 406 of ERISA and Section 4975 of the Internal Revenue Code.

Department of Labor News

Invalidation of Fiduciary Regulations

The Fifth Circuit has ruled that the Department of Labor's new standard for determining when a person providing "investment advice for a fee" is a fiduciary of an ERISA-governed plan or an IRA or HSA exceeded the Department's authority under ERISA.

The Department opted not to appeal that decision, but has not formally revoked the rules. Instead, the Department issued a non-enforcement policy stating that it will not take enforcement action against financial service providers working "diligently and in good faith to comply with the impartial conduct standards" in effect under the regulations' transition guidance for transactions that otherwise would now be subject to more demanding compliance standards under the "Best Interest Contract Exemption" or "Principal Transactions Exemption." The Department's Field Assistance Bulletin establishing the non-enforcement policy notes that it does not affect any rights of other potential parties, such as plan participants, to seek to enforce the regulations.

The Department has indicated that additional guidance will be forthcoming, but at present, in light of the Department's noncommittal approach to the Fifth Circuit decision, the regulatory landscape is now unclear. For the most part, financial institutions which had enacted protective measures for the purpose of complying with the rules are rolling those measures back, or at least considering doing so. Fidelity no longer accepts fiduciary responsibility for distribution counseling services, for example, having reverted to its pre-regulatory position that its activities consist of providing non-fiduciary investment education and not fiduciary advice. Likewise, Merrill Lynch has reversed its decision to discontinue commission-based IRAs. However, a Massachusetts federal district court recently expressed doubt that the Fifth Circuit's decision was binding nationwide. The court also allowed Massachusetts to proceed with a state-law regulatory proceeding based on Scottrade's alleged violation of its own internal policies adopted to comply with the new regulations.

While the Scottrade action is unusual, a number of states are also considering more direct legislative action to impose state-level fiduciary obligations on individuals offering financial advice. Finally, the SEC has taken the first steps toward adopting regulations of its own to address concerns about financial professionals, conflicts of interests, and customers' lack of understanding of when a financial professional is (and is not) obliged to act in the customer's best interest.

In light of the Fifth Circuit's invalidation of the regulations, plan fiduciaries should revisit their recordkeepers' marketing and participant counseling protocols. Fiduciaries need to determine whether the recordkeeper is a fiduciary, taking into account the pre-existing regulations and the possibility of continued validity of the new regulations. If the recordkeeper has taken on fiduciary status, the plan's fiduciaries need to be sure it has acknowledged this status, provided appropriate disclosures, and implemented appropriate safeguards. Regardless of whether the recordkeeper is or might be a fiduciary, the plan fiduciaries need to be sure they are comfortable with the quality of the services and communications offered, that there are protections against conflicts of interest, that associated compensation arrangements are reasonable, and that contractual indemnifications are appropriate in scope.

Continued Regulatory Focus on Retirement Plan Payment Deadlines

The Department of Labor and the IRS have continued to focus on whether plans are being proactive about meeting payment deadlines imposed by law and plan documents. Department of Labor auditors are seeking information about the payment outreach and missing participant search process for plans under their review, and Form 5500 requires disclosure of payments that were not made on time (excluding payments not made because the plan could not locate the individual despite diligent effort). IRS auditors are examining plans to determine whether the plans have met the legal deadlines for commencement of required minimum distributions. More information, along with suggestions for designing payment and missing participant search procedures, is available in our newsletter at https://www.hselaw.com/news-and-information/legalcurrents/1481-finding-and-paying-your-retirement-plan-participants.

Disability Claims Regulations

The Department of Labor's regulations requiring enhanced disclosures in connection with denial of claims for disability benefits took effect April 2, 2018. Plan sponsors and fiduciaries should make sure their plan documents, service contracts and communication materials have been updated and that claims are being processed in accordance with the new rules. While the regulations mostly affect insurance companies and disability claims administrators, large companies that administer ERISA-governed disability programs in-house also need to update their systems. In addition, retirement plans that offer enhanced vesting, early or enhanced payment, service credit, or other special benefits to disabled participants may also need to comply with the new rules, unless the plan relies entirely on the Social Security Administration or long-term disability plan administrator to determine a participant's disabled status. More information is available in our newsletter at https://www.hselaw.com/news-and-information/legalcurrents/1347-final-dol-disability-claims-procedure.

"ESG" Investing

For decades, the Department of Labor has taken the position that benefit plan fiduciaries must select investments and exercise the plan's proxy voting rights based on the economic best interests of participants. Only if all economic factors are equal can a plan consider non-economic considerations (such as environmental policies, or a desire for a diverse board of directors). In Field Assistance Bulletin 2018-01, the Department reiterated that position, and added that fiduciaries should not select an investment vehicle to serve as a qualified default investment alternative based on their policy preferences without regard to economic considerations or the possibly competing policy preferences of plan participants. Commentators generally perceived the tone of the Bulletin as disfavoring the taking into account of non-economic factors (often referred to as "ESG," or "environmental, social and governance" considerations). The Department also sounded a note of caution about a fiduciary decision to engage in shareholder activism, noting that its earlier statements in favor of exercising shareholder rights were not intended to imply that fiduciaries should routinely incur significant expenses to do so.

However, the Bulletin did acknowledge that in some circumstances, a factor that might normally just be an "ESG" factor might also have an economic impact that legitimately can or even must be taken into account. For example, a prudent fiduciary would not disregard the economic impact of a company's involvement in a major environmental disaster on its business prospects simply because environmental concerns are *also* an ESG factor. The Department also observed that a fiduciary can offer a fund with a "socially conscious" investment agenda if the investment option is cost-effective with competitive returns and does not require the plan to forego other opportunities.

While the Bulletin purports to be clarifying the Department's long-standing views, fiduciaries should take the Bulletin as a reminder that economic considerations must come first when making decisions about plan assets. To the extent a fiduciary concludes that considering topics that are not strictly economic is appropriate under ERISA (for example, because of the topic's economic implications in the circumstances, or because all economic factors are equal and the fiduciary has concluded that taking the ESG factor into account is appropriate for the plan), the fiduciary should be sure to document the reasons for that conclusion.

IRS News

New Employee Plans Compliance Resolution System Revenue Procedure

Revenue Procedure 2018-52 updates the IRS' Employee Plans Compliance Resolution System, the IRS' program allowing correction of errors involving qualified retirement plans, 403(b) plans and certain other tax-favored retirement programs. On September 28, 2018, the IRS released guidance modifying the Employee Plans Compliance Resolution System ("EPCRS"). The most significant change is that starting April 1, 2019, applicants using the Voluntary Correction Program ("VCP") will no longer be able to submit paper submissions. Instead, all VCP submissions must be made by using the electronic filing system and paying the IRS user fee through Pay.gov. The Pay.gov system will allow plan sponsors to authorize a legal representative to sign and submit a VCP submission on its behalf. If the plan sponsor chooses to authorize a legal representative to submit a VCP application on its behalf, it must sign a special penalty of perjury statement and a completed Form 2848 Power of Attorney and Declaration of Representative. The IRS expects to release updated instructions for VCP submissions in January 2019. Accordingly, Plan Sponsors should bear in mind to create a Pay.gov account this coming January and become familiar with the electronic filing system. Additionally, Plan Sponsors should coordinate with their finance departments to ensure that they are able to submit electronic payments through Pay.gov.

Student Loan Repayment 401(k) "Match"

The IRS issued a Private Letter Ruling ("PLR") to Abbott Pharmaceuticals, confirming that Abbott would not violate the "contingent benefit rule" (i.e., the general prohibition on benefits other than matching contributions being contingent on an employee's decision to make elective deferrals to a 401(k) plan) if Abbott made contributions to its retirement plan based on employees' student loan repayments. Under the PLR, Abbott's employees who meet specified requirements will be able to opt to have their student loan repayments taken into account for purposes of calculating Abbott's contributions to the 401(k) plan, instead of having Abbott match their elective deferrals. Employers considering such a program should bear in mind that:

- The PLR was issued only to Abbott, and no one else can rely on its content as binding guidance.
- Since Abbott's contributions are not based on elective deferrals, they are not considered "matching contributions" and are subject to a different type of nondiscrimination testing. An employer considering a program of this type will need to review its particular plan data to determine the extent to which a program like this would be feasible.
- Employers using a "safe harbor" design to satisfy certain nondiscrimination requirements would face special constraints, and likely will not be able to offer a student loan contribution *in lieu of* (rather than in addition to) a plan matching contribution.

402(g) Enforcement

The IRS has said that it will engage in enhanced outreach regarding employers' obligations to enforce the Section 402(g) limit on pre-tax and Roth contributions to their 401(k) plans, and will also increase its investigation and enforcement activities against individual taxpayers who violate these limits. Each plan sponsor should make sure their payroll and HRIS systems properly enforce the limits across all plans maintained by the employer and its controlled group affiliates, and that the rules for requesting and receiving timely refunds of excess contributions for individuals who exceeded the limit due to contributions to different employers' plans are communicated.

Use of Forfeitures to Fund QNECs, QMACs and Safe Harbor Contributions

The IRS has issued final regulations confirming its decision to allow plan forfeitures to be used to fund Qualified Nonelective Contributions ("QNECs"), Qualified Matching Contributions ("QMACs") and safe harbor 401(k) or 403(b) contributions. Employers were permitted to begin operating in accordance with the proposed regulations right away, without waiting for the regulations to be finalized, so long as their plan documents accommodate that course of action. As a general rule, vendors of IRS-pre-approved plans adopted the requisite amendments automatically, without the need for individual plan sponsor action. However, employers that took advantage of the new flexibility should check with their vendors to be sure their documentation is up to date.

The IRS has established March 31, 2020 as the deadline for 403(b) plans to have adopted plan documents that comply fully with the legal requirements applicable under Section 403(b) of the Internal Revenue Code. 403(b) sponsors should work with their vendors to make sure they will have a compliant document in place by this deadline. 403(b) sponsors should consider a pre-approved 403(b) plan document because the IRS does not offer a determination letter program for 403(b) plan sponsors.

In any event, since the process of drafting a compliant document or converting to a pre-approved document can involve a substantial amount of diligence regarding plan practices and will involve a careful review process to ensure accuracy, plan sponsors should consider beginning this process well before the March 31, 2020 deadline.

IRS Extends Nondiscrimination Relief for Frozen Defined Benefit Plans

Through the last plan year beginning before 2020, the IRS will continue to allow additional nondiscrimination testing flexibility for defined benefit plans that permit existing participants to continue earning benefits but are closed to new hires, if the plans satisfy specified requirements.

New Special Tax Notice

A plan administrator must provide any payee receiving an eligible rollover distribution with certain information about the tax consequences of the distribution and the distributee's rollover opportunities. The IRS has issued model notices for this purpose, and recently updated the models to reflect developments such as the loan rollover extension offered under the Tax Cuts and Jobs Act and 2016 IRS guidance on self-certifying eligibility for certain waivers of rollover deadlines. The new notices are included in IRS Notice 2018-74, available at https://www.irs.gov/pub/irs-drop/n-18-74.pdf.

Other News

State IRA Programs

State efforts to facilitate or mandate the availability of retirement savings programs continue to gain steam, and some states now have operational programs. Oregon's program has begun phasing in, and Illinois has a pilot program in operation, with California in the final stages of preparing its pilot program. Connecticut's program begins phasing in January 1st.

Oregon requires employers to file a certificate to obtain an exemption from the OregonSaves program for offering a qualified retirement plan, and to renew the exemption every three years. The deadlines to register for the program or file for exemption are:

- One hundred (100) or more Oregon employees: November 15, 2018
- At least fifty (50) but no more than ninety-nine (99) Oregon employees: May 15, 2019
- At least twenty (20) but no more than forty-nine (49) Oregon employees: December 15, 2019
- At least ten (10) but no more than nineteen (19) Oregon employees: May 15, 2019
- At least five (5) but no more than nine (9) Oregon employees: November 15, 2019
- Four (4) or fewer Oregon employees: May 15, 2020

Oregon settled a challenge to these filing requirements by the ERISA Industry Committee by agreeing to excuse its members from filing, and has indicated that it is working on a way to mine Form 5500 data to further limit the filing obligation. At present, however, the filing requirement remains relevant for non-ERIC members.

Illinois requires employers with 25 or more employees in Illinois who have been in business for at least two years and have not offered a qualified retirement plan in the preceding two years to offer the Secure Choice Savings Program. The State will notify employers directly when they will be required to register or indicate that they are exempt. The timeline is scheduled as follows:

- Five hundred (500) or more Illinois employees: November 1, 2018
- At least one hundred (100) but no more than four hundred ninety-nine (499) Illinois employees: July 1, 2019
- At least twenty-five (25) but no more than ninety-nine (99) Illinois employees: November 1, 2019

The Illinois Governor has issued an amendatory veto that makes the Secure Choice program permissive, rather than mandatory. It is unclear whether the veto will stand or whether the Illinois legislature will override it (which may not occur until November, when the body is scheduled to be in session next).

The New York City Council has proposed to establish a "Savings Access New York Retirement Program" that would require New York City employers with 10 or more employees who have been in business for at least two years and do not offer a qualified retirement plan to offer the new savings program. The proposal is currently in committee, and no action has been taken to date.

Church Plan Funding Challenges

Religiously affiliated organizations (particularly hospitals) that have claimed exemptions from pension funding law on the grounds of "church plan" status continue to face court challenges. Although district courts have largely sided with the defendants, plaintiffs recently were allowed to proceed with a case challenging Dignity Health's "church plan" status, and some lawsuits have settled. Ultimately, religiously affiliated pension plan sponsors and any organization considering acquiring or partnering with such an organization that has an underfunded pension plan should understand the potential liabilities associated with the underfunding. Plan sponsors should bear in mind, as well, that regardless of the likelihood of a successful federal lawsuit, underfunded pension plans can create significant drains on an organization's resources, and may result in adverse publicity for the organization and challenges to employee morale.

Furthermore, "church plan" sponsors remain subject to state law, and courts have permitted former employees of St. Anthony Medical Center and Dignity Health to proceed with state law claims in relation to insufficiently funded pension benefits. Accordingly, "church plan" status may be at least as much a curse as a blessing, depending on the applicable state's law and the plan's circumstances.

Finally, employers must bear in mind any contractual obligations they may have and the enforcement rights that employees or unions may have on connection with those contracts. The judge in the St. Anthony case cited contractual claims based on the plan document as well as a state law breach of fiduciary claim.

Employee Ownership

The John S. McCain National Defense Authorization Act included provisions intended to facilitate the creation of employee stock ownership plans ("ESOPs") and worker-owned cooperatives by relaxing the requirements governing Small Business Administration loans to facilitate these transactions. However, recent proposed regulations by the Small Business Administration indicate that SBA approval for such transaction will continue to be reviewed on a case-by-case basis. Regardless of the SBA's involvement, an employer considering an ESOP should discuss the significant risks and potential future operating and liquidity constraints with experienced ERISA counsel before proceeding.

Multiple-Employer Retirement Plans

The Department of Labor has proposed regulations intended to facilitate "multiple-employer" retirement plans covering unrelated employers. Proposals to promote these arrangements also have circulated in Congress. While multiple-employer programs currently are permissible and in use (mostly by smaller companies seeking a cost-effective retirement solution and/or using Professional Employer Organizations that offer these plans), existing guidance restricts employers' ability to outsource the fiduciary functions associated with these plans, somewhat limiting their appeal and utility.

Concededly, joining a multiple-employer structure may facilitate small employers' ability to offer retirement plans by allowing them to outsource administrative responsibilities and obtain access to more cost-effective investments. Nonetheless, employers should be sure they understand the disadvantages as well as the advantages of these programs before deciding to enroll. These programs may allow less flexibility than an independent program, and may make it cumbersome to leave a Professional Employer Organization, change plan contribution obligations or discontinue the plan, or otherwise redesign a company's human resources offerings. In addition, involvement in such a plan may complicate the potential for a sale of the company or at least result in a more complicated sale negotiation and post-sale integration process.

Cybersecurity

Concerns about the security of the reams of sensitive data maintained by benefit plans and their sponsors and vendors continue to rise in the wake of well-publicized data breaches. The Internal Revenue Service has initiated an active campaign aimed at educating tax professionals (including benefit plan service providers) about cybersecurity safeguards (see https://www.irs.gov/newsroom/protect-your-clients-protect-yourself-tax-security-101). Best practices in contracting, security audits and other aspects of this field continue to evolve. Benefit plan fiduciaries should work with their data security advisers to be sure that the plan sponsor and vendors maintain appropriate security precautions, and that their plans' vendor contracts establish prudent standards of conduct and provide for the desired level of insurance coverage and indemnity protection in the event of a breach.

Association Retirement Plans

Both the Department of Labor and the Treasury Department are in the process of preparing regulations intended to facilitate the operation of multiple employer retirement plans for unrelated employers.

PBGC Plan Termination Regulations

The PBGC issued final regulations reflecting Pension Protection Act changes to the rules for guarantees applicable to certain business owners' pensions if an underfunded plan terminates. Generally, the statutory changes reflected in the new regulations allow owner-employees earlier and greater access to their pension benefits than was previously the case. The regulations also permit simplification of pension calculations while a distress termination is pending.

Puerto Rico

Employers that maintain retirement plans for employees in Puerto Rico must satisfy the requirements of Puerto Rico's tax laws, even if the plan also satisfies U.S. Internal Revenue Code requirements. Puerto Rico passed legislation in early 2017 that alters some of those requirements, although aspects of that legislation were subsequently amended by further legislation, and additional legal changes are expected. If you have a retirement plan covering employees in Puerto Rico, regardless of whether it is a Puerto Rico only plan or a "dual qualified" plan that also covers U.S. employees, consult Puerto Rico counsel about your obligations.

For More Information

As always, please feel free to contact a member of the Employee Benefits & Executive Compensation group for more information about the items discussed in this newsletter, or for assistance in other matters, at 585.232.6500 or visit www.hselaw.com.

Updated Internal Revenue Code and Other Statutory Limits

	2019	2018
IRA Contribution Limit	$6,000	$5,500
IRA Catch-Up Contributions	$1,000	$1,000
Joint Return	$103,000	$101,000
Single or Head of Household	$64,000	$63,000
SEP Minimum Compensation	$600	$600
SEP Maximum Contribution	$56,000	$55,000
SEP Maximum Compensation	$280,000	$275,000
SIMPLE Maximum Contributions	$13,000	$12,500
Catch-up Contributions	$3,000	$3,000
Annual Compensation	$280,000	$275,000
Elective Deferrals	$19,000	$18,500
Catch-up Contributions	$6,000	$6,000
Defined Contribution Limits	$56,000	$55,000
ESOP Limits	$1,130,000 $225,000	$1,105,000 $220,000
HCE Threshold	$125,000	$120,000
Defined Benefit Limits	$225,000	$220,000
Key Employee	$180,000	$175,000
457 Elective Deferrals	$19,000	$18,500
Control Employee (board member or officer)	$110,000	$110,000
Control Employee (compensation-based)	$225,000	$220,000
Taxable Wage Base	$132,900	$128,400
Health Care FSA Salary Reduction Maximum	TBD	$2,650
Individual Out-pocket Maximum Limit under the Affordable Care Act	$7,900	$7,350
Family Out-pocket Maximum Limit under the Affordable Care Act	$15,800	$14,700
High Deductible Health Plan and Health Savings Account (“HSA”) Limits		
Min. Individual Deductible	$1,350	$1,350
Min. Family Deductible	$2,700	$2,700
Individual Out-pocket Maximum Limit	$6,750	$6,650
Family Out-pocket Maximum Limit	$13,500	$13,300
Individual HSA Contribution Limit	$3,500	$3,450
Family HSA Contribution Limit	$7,000	$6,900
HSA “Catch-up” Contribution Limit	$1,000	$1,000