Employee Benefits News

Winter 2014

KUTAK ROCK LLP

KUTAK ROCK EMPLOYEE BENEFITS & EXECUTIVE COMPENSATION GROUP CONTACTS

John E. Schembari
John.Schembari@KutakRock.com

Michelle Ueding
Michelle.Ueding@KutakRock.com

Alfred "Mike" Fowler
Mike.Fowler@KutakRock.com

Shira B. McKinlay
Shira.McKinlay@KutakRock.com

William C. McCartney
William.McCartney@KutakRock.com

P. Brian Bartels
P.Brian.Bartels@KutakRock.com

Andreia G. Rosa
Andreia.Rosa@KutakRock.com

Alexis Kramer
Alexis.Kramer@KutakRock.com

Jeffrey J. McGuire
Jeffrey.McGuire@KutakRock.com

Kutak Rock Locations
Atlanta
Chicago
Denver
Fayetteville
Irvine
Kansas City
Little Rock
Los Angeles
Minneapolis
Oklahoma City
Omaha
Philadelphia
Richmond
Scottsdale
Spokane
Washington, D.C.
Wichita

www.KutakRock.com

Two Attorneys Join Employee Benefits Group

Mr. Bartels

Brian Bartels is a 2008 graduate of Creighton University School of Law, where he was a member of the *Creighton Law Review*. He joined our group in May to primarily assist our clients on health and welfare matters. Since 2010, Mr. Bartels has worked closely with clients on questions regarding the Affordable Care Act and its implementing regulations. He also has experience advising clients on employee benefit issues in the context of mergers and acquisitions.

Mr. McGuire

Jeffrey McGuire is a recent graduate of the University of Nebraska College of Law, where he served as Articles Editor of the *Nebraska Law Review*. Mr. McGuire joins us from a small Omaha firm, where he gained experience in employee benefits compliance and taxation. He will assist all the attorneys in the Employee Benefits and Executive Compensation Group, with a focus on retirement plans.

The Headlines Say—

"Fidelity sued by employees over its own 401(k) plan"

"US Labor Department reaches $5.25M settlement with GreatBanc Trust"

"Great-West Financial Acquires J.P. Morgan Retirement Plan Services"

"Schwab shoos 25 billion of client assets out the door"

"John Hancock Ducks ERISA Suit Alleging Excessive Plan Fees"

Every week, it seems, another news story mentions a retirement plan service provider getting sued, audited or purchased. Key executives often resign or the service provider may exit or enter a new line of business. This is all just background noise or fodder for fiduciary training—until the service provider in question is yours. What should you do when your service provider is in the news? We recommend the following:

1. **Acknowledge the situation**. The fiduciary in charge of hiring and firing service providers has an obligation to monitor the service provider, and this includes watching the news. Most of the time, the applicable fiduciary is a retirement committee. The retirement committee may meet quarterly and discuss an investment "watch list." A fiduciary committee in charge of plan administration and monitoring service providers should also have a "watch list." We often refer to this "watch list" as a legal report; it contains relevant industry news, recent case law and new regulations and guidance from the IRS, DOL and PBGC. A prudent fiduciary process should include a regular report on these items. The committee should document its review of the news in its meeting minutes.

2. **Evaluate the news**. Not all bad news is relevant and not all favorable court decisions are irrelevant. The fact is that some service providers are so large and prominent that the rule of averages indicates they will eventually be involved in a lawsuit. However, reviewing the allegations and defenses may show a fiduciary where to focus its attention or teach a fiduciary that its service provider has a different-than-expected view of its obligations. Receiving a report is not enough. As in most fiduciary practices, demonstrating due diligence and procedural prudence matters. We recommend asking:
   a. Do I understand the facts?
   b. Do the facts impact my plan (i.e., are we in the same situation)?
   c. If not, am I comfortable with my service provider's behavior from an ethical perspective?
   d. Does this tell me something new about my provider (e.g., that it does not consider itself a fiduciary with respect to a particular service it provides)?
3. **Make a decision.** Every committee discussion should end with a decision. Sometimes, the decision is to do nothing or wait. Here are some illustrations:
   a. A service provider lawsuit involves an operational practice that impacts all plans using that service provider. A committee discusses the allegations and the practice; determines the service provider discontinued the practice with respect to its plan; evaluates whether its plan was harmed; discusses merits and costs of its own suit regarding the prior practice; and resolves to monitor the pending class-action lawsuit.
   b. An article regarding its service provider causes a committee concern about its service provider's ethics, and the committee resolves to request a response from its service provider regarding the committee's concerns.
   c. A lawsuit against a service provider is dismissed; however, the plan sponsor of the impacted plan is found to have breached its fiduciary duty. A committee of a plan with the same service provider reviews the case and determines (i) the service provider defended the case in the manner expected, and (ii) the other plan sponsor's failure to take certain actions (taken by the reviewing committee) caused it to breach its fiduciary duties. The committee resolves to do nothing.
4. **Document everything.** Committee meeting minutes work well if the matter was discussed at a meeting. If something happens between meetings, many committee charters allow conducting business via e-mail. Either way, the written record should contain: (i) what the committee reviewed; (ii) what questions the committee asked and the answers received; (iii) the decision made, including any further action; and (iv) the rationale or basis for the decision.

by Michelle Ueding

DOL Releases Guidance on Missing Participants in Terminated DC Plans

The Department of Labor issued Field Assistance Bulletin 2002-04 to assist fiduciaries of terminated defined contribution plans in locating missing participants and properly distributing the participants' accounts benefits. While the guidance applies specifically to terminated defined contribution plans, it is the first guidance for locating missing participants since the Internal Revenue Service and the Pension Benefit Guaranty Corporation cancelled their respective locator programs.

The following steps must be taken to locate a missing participant:

- Use certified mail;
- Check related plan and employer records;
- Check with designated plan beneficiaries; and
- Use the electronic search tools.

If the missing participant cannot be located, plan fiduciaries will have to select a distribution method. The preferred approach would be to roll over funds to an IRA. A plan fiduciary may charge missing participants' accounts reasonable expenses for efforts to locate them.

by Andreia Rosa

How Companies Can Use SUB-Pay Plans to Save Money on Severance Payments

In the face of increasing national and international competition, many companies are regularly assessing their operations for ways to reduce expenses and improve profitability. Often, these assessments result in layoffs or other types of downsizing. If a company offers severance payments to those affected by the layoffs or downsizing, SUB-Pay plans offer a cost-effective means of providing severance. In many cases, SUB-Pay plans can save companies in excess of 45% of the total cost of severance payments.

Traditional Severance Plans Are Tax-Inefficient

U.S. companies that lay off employees or expect to lay off employees in the future as a result of a merger, acquisition, business realignment or seasonal employment often offer severance benefits to affected employees. The traditional severance plan is paid as taxable compensation to the former employees and is subject to state and federal income tax, as well as Social Security and Medicare taxes (“FICA”). Traditional severance plans are also not typically coordinated with many states’ unemployment insurance (“UI”) benefits. As a result, traditional severance benefits are typically taxed at preseverance tax rates and may result in companies losing the opportunity to coordinate benefits with state aid.

What Is a SUB-Pay Plan?

Introduced by the IRS in 1956, Supplemental Unemployment Benefit Payment (“SUB-Pay”) Plans are a unique type of severance plan designed to assist employees engaging in an involuntary termination due to a reduction in force, job elimination, reorganization or a similar circumstance. With a SUB-Pay Plan, employers save payroll tax dollars because SUB-Pay plans are exempt from FICA taxes. In addition, SUB-Pay Plans enable companies to utilize their paid-in asset of state UI taxes to supplement state UI benefits with the separation pay offered by the company.

SUB-Pay Plans were in the news recently, as the Supreme Court issued its decision in the *Quality Stores* case. In *Quality Stores*, the Supreme Court reaffirmed the long-standing belief that traditional severance payments are generally subject to FICA and FUTA taxes. However, the Supreme Court also held that properly structured SUB-Pay Plans are not subject to these same taxes.

Summary of SUB-Pay Benefits

Benefits to the Employer

- Plans are customized based upon the specific financial and cultural objectives of each business;
- Save a minimum of 7.65% in severance costs from FICA tax savings and as much as 45% when state UI benefits are coordinated with separation pay;
- Payments are exempt from FUTA and SUTA taxes; and
- Reduce the impact of severance costs on the company’s cash flow since SUB-Pay benefits are required to be made on a periodic basis.

Benefits to the Former Employee

- SUB-Pay Plans can provide 7.65% more separation pay because SUB-Pay is not subject to FICA tax; and
- SUB-Pay Plans are paid on a periodic basis which provides the former employee with steady income during transition to reemployment and may reduce the additional tax burden associated with lump-sum severance payments.

Next Steps

If your company is considering layoffs or downsizing in the future, it is worth your time to investigate SUB-Pay Plans as a means of benefiting the company and your former employees. SUB-Pay Plans can provide meaningful benefits for layoffs involving as few as 50 employees. Obviously, the more employees involved and the more states in which the layoffs occur, the greater the opportunity for meaningful savings to the company and the employees.

by John Schembari

Permitted Election Changes in Cafeteria Plans

Section 125 cafeteria plan rules have long required that elections under a cafeteria plan be irrevocable except to the extent permitted under specific optional mid-year election change rules adopted by the plan. In order to accommodate some of the changes brought about under the Affordable Care Act ("ACA"), the Treasury Department issued IRS Notice 2014-55 (the "Notice"), allowing significant changes to cafeteria plan permitted election change rules. This guidance became immediately effective upon the Notice's issuance (September 18, 2014).

Background

Previously, employees in a cafeteria plan were permitted to make mid-year election changes if they had a change in status that corresponded with such election change. In addition, employees could change elections upon the occurrence of a "special enrollment" event, including loss of other coverage or certain family events. The Notice expands the permitted election change rules to take into account both Employer Shared Responsibility rules and the interaction with the new Health Insurance Marketplace (the public health insurance exchanges).

Permitted Election Change Corresponding With Employer Shared Responsibility Rules

Under Employer Shared Responsibility rules, applicable large employers who do not provide group health coverage to their full-time employees may be subject to a penalty. In the event certain employees are determined to be full-time, they must be offered coverage for a period of time in the future, even if their hours are reduced. This provided a problem for employees whose hours are reduced, but who may not want to maintain coverage under the employer's plan following such reduction in hours. Under the cafeteria plan regulations, loss of coverage was required before a mid-year election change was permitted.

The Notice specifically permits employees who are reasonably expected to work 30 hours or more per week to prospectively revoke their coverage under a cafeteria plan if their employment status changes, so that, following the change, they are reasonably expected to work less than 30 hours per week. This mid-year revocation of coverage must correspond to the enrollment of the employee (and any applicable dependents) in another minimum essential coverage plan. The new coverage must start no later than the first day of the second month following the month the original coverage is revoked.

Permitted Election Change Corresponding With Marketplace Enrollment

Under existing cafeteria plan regulations, an employee would be unable to revoke an existing election mid-year solely in order to enroll in a plan under the Health Insurance Marketplace ("Marketplace"). This presents particular difficulties for employees with non-calendar-year plans. In such case, Marketplace open enrollment does not correspond to open enrollment under their employers' plans. The rules under the current regulations that would allow participants to make new elections mid-year that correspond with special enrollment rights under another plan do not extend to special enrollment rights under the Marketplace.

The Notice resolves this issue by permitting prospective mid-year election changes so that an employee can revoke participation in an employer plan in order to obtain Marketplace coverage. If an employee is eligible for special enrollment mid-year into a Marketplace plan, or if the employee wants to enroll in a Marketplace plan during the Marketplace open enrollment period, the cafeteria plan may allow the employee to revoke his or her coverage under the employer's plan. The revocation must correspond to the new coverage on a Marketplace plan, and such coverage must be effective no later than the day after the last day of coverage through the employer's plan.

Timing of Written Amendment

A cafeteria plan must be amended to allow for these mid-year election changes on or before the last day of the plan year in which the elections are allowed. For 2014 plan years only, the plan may be amended before the last day of the plan's 2015 plan year.

by Shira McKinlay

Nonqualified Deferred Compensation Compliance More Important Than Ever

TIME FOR REVIEW

Nonqualified deferred compensation ("NQDC") arrangements are governed by Internal Revenue Code ("Code") Section 409A and, potentially, the Employee Retirement Income Security Act of 1974 ("ERISA"). Making sure your NQDC arrangement is in compliance with applicable law has never been so important in light of recent legal developments affecting those arrangements.

Audit Initiative

In May, the IRS announced that it had launched an NQDC audit initiative (the "Initiative") to gauge compliance with Code Section 409A. While this Initiative is intended to be limited in scope, the IRS has stated part of its intent for the Initiative is to develop a Code Section 409A audit strategy which, presumably, would be used for expanded future audits of NQDC arrangements. The Initiative is intended to test compliance with Code Section 409A in three particular areas: (i) initial deferral elections; (ii) subsequent deferral elections; and (iii) plan distributions.

Correction of Plan Errors

When NQDC arrangements violate Code Section 409A, there are two self-correction programs offered by the IRS, but they are limited in nature. Only certain enumerated errors can be corrected and only for a limited time after an error occurs. Earlier this year we participated in a conference where IRS agents provided their unofficial opinions on various Code Section 409A issues. One agent stated that the correction programs are designed to be limited in scope and violations outside the programs should result in tax penalties. Therefore, it is important to make sure errors are discovered timely and corrected as quickly as possible.

ERISA Compliance

The Fifth Circuit Court of Appeals recently held that an NQDC arrangement was subject to ERISA even though the express purpose of the plan was not to provide retirement income. The court noted that a "pension plan" under ERISA is defined as:

> any plan, fund, or program . . . maintained by an employer . . . to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program (i) provides retirement income to employees, or (ii) results in a deferral of income by employees for periods extending to the termination of covered employment or beyond, regardless of the method of calculating the contributions made to the plan, the method of calculating the benefits under the plan or the method of distributing benefits from the plan . . . .

The court noted that the NQDC plan at issue referred to itself as a "deferred compensation plan" that allowed employees to "defer receipt of a portion of their compensation to be earned with respect to the upcoming Plan Year." Further, the plan contemplated employees deferring income to termination of employment or beyond. The court, therefore, held the plan to be a "pension plan" as it fell into the second condition under ERISA.

Many NQDC arrangements are also "top-hat plans" under ERISA, meaning they are unfunded and maintained "primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees." Top-hat plans are exempt from many of ERISA's requirements but still must comply with ERISA in several ways. Therefore, regardless of whether your plan qualifies as a top-hat plan, the question of whether your NQDC arrangement is subject to ERISA is still important.

Conclusion

Given these recent developments, it is more important than ever to make sure your NQDC arrangements are in compliance with applicable law. Employers with NQDC arrangements should have their arrangements and their plan procedures reviewed for compliance with Code Section 409A and ERISA. If you would like your NQDC arrangement reviewed, please contact your Kutak Rock LLP attorney or a member of our Employee Benefits and Executive Compensation Practice Group.

by William McCartney

Newsworthy Items

Reach of Contraceptive Mandate Following Hobby Lobby. The Supreme Court's decision in *Burwell v. Hobby Lobby* provided that closely held for-profit corporations are not required to pay for contraceptives if doing so would violate the corporation's sincerely held religious beliefs. Since the case was decided this summer, the government issued proposed regulations which would allow for more types of employers, such as closely held for-profit entities that do not have a religious affiliation, to opt out of paying for some or all contraceptives under their health plans.

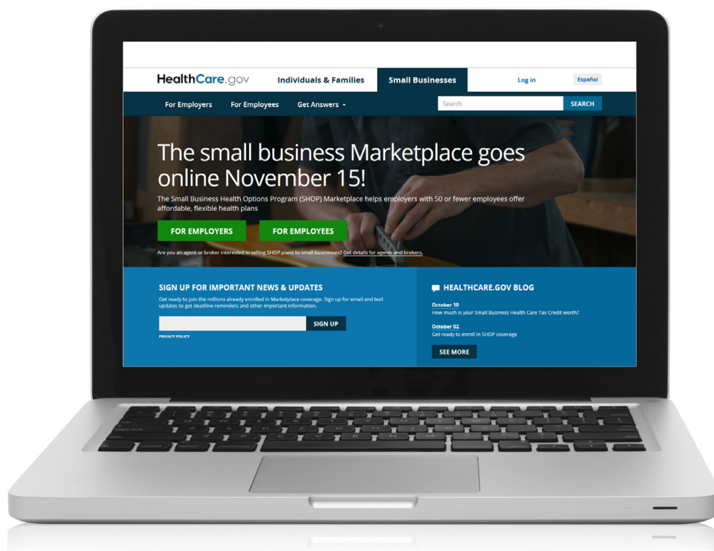
2015 Health Savings Account Increases. The IRS adjusted its maximum annual Health Savings Account ("HSA") contribution limits for the 2015 tax year. The annual limit for an individual with self-only coverage under a high-deductible health plan is $3,350 (an increase of $50 from 2014). Individuals with family coverage under a high-deductible health plan can contribute up to $6,650 (an increase of $100 from 2014) per year.

Cities & States Pass Paid Leave Laws. In September, California joined Connecticut, the District of Columbia and 12 cities in passing legislation requiring certain employers to provide paid sick leave to their employees. We anticipate this trend will continue, as New Jersey and several cities are poised to pass similar laws in the near future.

Employer Sued Over Wellness Program. The EEOC filed suit against a Wisconsin-based company, claiming it violated the Americans with Disabilities Act when it required employees to complete a biometric test and health risk assessment. When one employee failed to do so, the company canceled his medical insurance and required him to pay 100% of his monthly premiums. The EEOC believes that the test and assessment were disability-related inquiries and medical examinations in disguise and, due to the steep penalties for nonparticipation, not truly voluntary.

2015 Cost-of-Living Increases. The IRS announced its annual cost-of-living adjustments for qualified retirement plans for the 2015 tax year. These adjustments affect the amount of benefits payable and contributions allocable under qualified retirement plans. A chart of the 2015 limitations can be found at: http://www.kutakrock.com/2015-cola-chart/.

Soft Launch of SHOP Marketplace & Open Enrollment. In late October, the Small Business Health Options Program ("SHOP") Marketplace opened to small employers (those with 50 or fewer full-time equivalents) in five states. The goal is to fix any problems encountered by users in Delaware, Illinois, Missouri, New Jersey and Ohio prior to November 15, when the SHOP Marketplace opens to all other states on the federal platform. Also on November 15, the federal individual Marketplace will commence its second open enrollment period. Open enrollment will run through February 15, 2015.



Windsor Amendments Required Before Year-End. Since June 26, 2013, the IRS has required retirement plans to treat same-sex couples as married if the couple was lawfully married under the

laws of one of the 50 states, the District of Columbia, or a foreign jurisdiction. Sponsors of Code § 401(a) qualified plans (e.g., 401(k), defined benefit) have until December 31, 2014 to amend their plans' definition of "spouse." We also recommend plan sponsors discuss operational compliance with their plan service providers.

HATFA Elections Required Before Year-End. Passage of the Highway and Transportation Funding Act ("HATFA") earlier this year extended the application of interest rate smoothing provisions to defined benefit pension plans. HATFA automatically applies higher assumed interest rates to 2013 plan years, unless plan sponsors affirmatively opt out of the law. To opt out of HATFA with respect to the 2013 plan year, plan sponsors can either provide written notice to the plan's actuary and the plan administrator by December 31, 2014 (for calendar-year plans) or file a Form 5500 series that reflects MAP-21 rates by December 31, 2014. Plan sponsors may also want to consider modifying prefunding balances for 2014 and redesignating contributions between the 2013 and 2014 plan years.

Employer Mandate. Beginning in 2015, large employers (those with 100 or more full-time equivalents) may be subject to a penalty if they do not offer medical coverage to full-time employees that provides minimum essential coverage, is affordable and meets minimum value requirements. Under transition relief issued in February, large employers must offer minimum essential coverage to 70% of their full-time employees and their dependent children to avoid the penalty; a 95% threshold will apply in 2016.

Cycle D Filing. In accordance with the IRS cyclical process for submitting an individually designed retirement plan for a determination as to its tax-qualified status under the Internal Revenue Code, employers in "Cycle D" must submit their qualified plans to the IRS no later than January 31, 2015. Generally, multiemployer plans and plans maintained by employers with employer identification numbers ending in either 4 or 9 are Cycle D eligible.

Supreme Court Granted Certiorari in *Tibble v. Edison*. ERISA allows plan participants to bring suit for breach of fiduciary duties, as long as suit is brought within the six-year statute of limitations. In *Tibble*, plan fiduciaries chose higher-fee, retail-class mutual funds as plan investments when identical, lower-fee mutual funds were available. The Supreme Court will decide whether plan participants can challenge this fiduciary decision, which was made more than six years before filing suit, if those decisions could have been reconsidered during the six-year time period.

by Alexis Kramer

The members of the Employee Benefits and Executive Compensation Practice Group regularly speak to plan sponsors, trustees, fiduciaries and others on legal issues and developments. The following list of recent speeches, while not exhaustive, highlights many of the areas where Kutak Rock Employee Benefits and Executive Compensation attorneys have been asked to speak across the country during 2014.

Best Practices for ESOP Fiduciaries, Omaha, NE, November 11, 2014

Revisiting Fiduciary Responsibilities in Public Sector Plans, Boston, MA, October 13, 2014

Affordable Care Act Essentials, Lincoln, NE, September 24, 2014

Executive Deferred Compensation, ESOP Association, Midwest Conference, Chicago, Oak Brook, IL, September 12, 2014

The Affordable Care Act for Employers, Denver Business Series, Denver, CO, August 14, 2014

Pension Guarantee Funds in Different Countries, Chicago, IL, June 24, 2014

The Affordable Care Act's Impact on Employee Benefit Plans, Omaha, NE, May 15, 2014

Affordable Care Act Essentials, Ashland, NE, May 1, 2014

Affordable Care Act Update, Omaha, NE, April 30, 2014

Employee Benefits and Executive Compensation Group

Kutak Rock LLP's Employee Benefits and Executive Compensation Practice Group serves clients with respect to legal matters concerning employee benefits and executive compensation. The group's collective legal expertise provides clients with thorough representation in virtually every aspect of employee benefits matters. Our employee benefits and executive compensation clients range from small, closely held organizations to international, publicly traded corporations to city and state governments. For more information, visit us online at www.KutakRock.com.

John E. Schembari
John.Schembari@
KutakRock.com

Michelle Ueding
Michelle.Ueding@
KutakRock.com

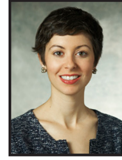
Alfred "Mike" Fowler
Mike.Fowler@
KutakRock.com

Shira B. McKinlay
Shira.McKinlay@
KutakRock.com

William C. McCartney
William.McCartney@
KutakRock.com

P. Brian Bartels
P.Brian.Bartels@
KutakRock.com

Andreia G. Rosa
Andreia.Rosa@
KutakRock.com



Alexis Kramer
Alexis.Kramer@
KutakRock.com

Jeffrey J. McGuire
Jeffrey.McGuire@
KutakRock.com

Employee Benefits News is a publication of Kutak Rock LLP and is intended to notify our clients and friends of current events and to provide general information about employee benefits issues. It is not intended, nor should it be used, as legal advice, and it does not create an attorney-client relationship. This publication may be considered advertising in some states. The determination of the need for legal services and the choice of a lawyer are extremely important decisions and should not be based solely upon advertisements or self-proclaimed expertise.

To ensure compliance with requirements imposed by the IRS, we inform you that any federal tax information contained in this communication should not be used or referred to in promoting, marketing or recommending any entity, investment plan or arrangement, and such advice is not intended to be written or used, and cannot be used, by a taxpayer for the purpose of avoiding penalties under the Internal Revenue Code.

Atlanta
Suite 2750
303 Peachtree Street, NE
Atlanta, GA 30308
404-222-4600

Chicago
Suite 2050
One South Wacker Drive
Chicago, IL 60606
312-602-4100

Denver
Suite 3000
1801 California Street
Denver, CO 80202
303-297-2400

Fayetteville
Suite 200
234 East Millsap Road
Fayetteville, AR 72703
479-973-4200

Irvine
Suite 1500
5 Park Plaza
Irvine, CA 92614
949-417-0999

Kansas City
Suite 800
Two Pershing Square
2300 Main Street
Kansas City, MO 64108
816-960-0090

Little Rock
Suite 2000
124 West Capitol Avenue
Little Rock, AR 72201
501-975-3000

Los Angeles
Suite 4550
777 South Figueroa Street
Los Angeles, CA 90017
213-312-4000

Minneapolis
Suite 1750
U.S. Bank Plaza South
220 South Sixth Street
Minneapolis, MN 55402
612-334-5000

Oklahoma City
Suite 475
6305 Waterford Boulevard
Oklahoma City, OK 73118
405-848-2475

Omaha
The Omaha Building
1650 Farnam Street
Omaha, NE 68102
402-346-6000

Philadelphia
Suite 28B
Two Liberty Place
50 South Sixteenth Street
Philadelphia, PA 19102
215-299-4384

Richmond
Suite 800
Bank of America Center
1111 East Main Street
Richmond, VA 23219
804-644-1700

Scottsdale
Suite 300
8601 North Scottsdale Road
Scottsdale, AZ 85253
480-429-5000

Spokane
Suite 1700
Bank of America Financial Center
601 West Riverside Avenue
Spokane, WA 99201
509-747-4040

Washington, D.C.
Suite 1000
1101 Connecticut Avenue, NW
Washington, DC 20036
202-828-2400

Wichita
Suite 150
1605 North Waterfront Parkway
Wichita, KS 67206
316-609-7900