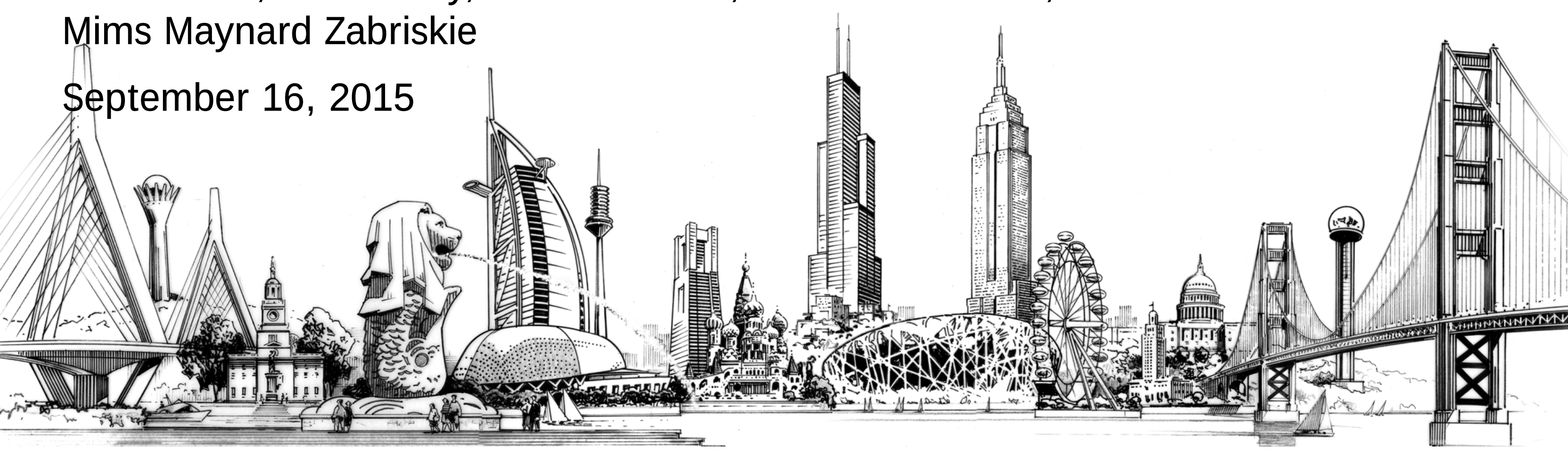
Morgan Lewis

HOT TOPICS IN EMPLOYEE BENEFITS: WHAT WE'RE SEEING

Presenters: Amy Pocino Kelly (moderator), Andy Anderson, Lisa Barton, Althea Day, Brian Ortelere, Michael Richman, Mims Maynard Zabriskie

September 16, 2015



Agenda

- Health and Welfare
- Fiduciary Considerations
- Plan Sponsor Considerations
- ERISA Litigation
- Executive Compensation
- Multiemployer Plans

PRESENTER: ANDY ANDERSON

HEALTH AND WELFARE

ACA Reporting

- In full song for 2015 after *King v. Burwell*
  - No practical hope for a delay or postponement until 2016
- Reporting to individuals by January 31 (Feb. 1 for 2016)
- Reporting to IRS by February 28 (Feb. 29 for 2016) (March 31 if electronic)
- Recently expanded FAQs, final 2015 forms, final 2015 instructions
- Allows IRS to monitor and act on ACA:
  - Individual mandate (Code Section 6055/Form 1095-B)
  - Employer shared responsibility exposure (Code Section 6056/Form 1095-C)
  - Exchange subsidy eligibility (Code Section 35/both forms)

ACA Reporting

- Recent developments:
  - Vendors reporting little to no ability to help new customers
  - Expanded FAQs create COBRA headaches and guarantee corrected forms
  - Final instructions:
    - Significantly ease multiemployer reporting tasks
    - Offer “no questions asked” 30-day extension and the possibility of a second 30-day extension
    - Highlight significantly increased penalty structure
    - Outline when good faith efforts will eliminate penalties
- Morgan Lewis Webinar, “ACA Reporting—Nuts And Bolts,” October 28, 2015

Domestic Partners

- All states must now issue marriage licenses to same-sex couples and fully recognize same-sex marriages lawfully performed out of state
- As such, is there a long-term health and welfare role for domestic partner status?
- Background:
  - Domestic partner status was created by employers to establish an indicia for health plan eligibility (often drawn from common-law marriage concepts)
    - Led to "home brew" domestic partner affidavits
    - Sometimes resulted in same- and opposite-sex domestic partner status due to issues of fairness or competitive pressures
  - Domestic partner registries then spread among states and local entities
  - Can result in state and federal imputed income consequences if domestic partner is not a dependent for the purpose of tax-free health coverage
  - Domestic partner coverage is sometimes required under state or local contracting ordinances

Domestic Partners

- Considerations:
  - Marriage now available to everyone..........but other protections (employment, housing, partner's employer beliefs) have not yet caught up
    - Watch for Executive Agency actions during remaining Obama term
  - Internal equity, "take away" or competition concerns
    - Might your organization now be exposed to claims of preferential treatment (particularly if your organization does not recognize opposite-sex domestic partners)?
    - Have domestic partner benefits become an expectation in your organization?
  - When to end domestic partner coverage, communicate, and how much time to give employees to react?
  - Is the administrative complication worth the return?
  - Might there be state or local contracting considerations or employment law concerns?
- Ultimately, lack of "need" may not trump organizational issues surrounding continuing domestic partner benefits..............

PRESENTER: MICHAEL RICHMAN

FIDUCIARY CONSIDERATIONS

Fiduciary Considerations – DOL Investment Advice Fiduciary Regulation

- Background
  - 1974 – ERISA enacted – includes “investment advice” in fiduciary definition
  - 1975 – To address industry and SEC concerns, Department of Labor (DOL) regulation creates “five-part test” to define “investment advice”
  - 2010 – DOL proposes extensive changes to its 1975 regulation
  - 2011 – DOL announces it will withdraw and repropose the changes
  - April 2015 – DOL publishes its reproposal

Current Developments

- Initial comment period – closed July 21
- DOL hearing – four days (Aug. 10-13), more than 70 witnesses
  - Testimony both in support of and opposing the changes
  - Hearing transcript posted on DOL website Sept. 8
- Reopened comment period – closes Sept. 24
- Congressional hearings and legislative proposals
- When/if finalized (based on current provisions) –
  - Effective date – 60 days after publication
  - Applicability date – eight months after publication
  - Many commenters requested an extended transition period

PRESENTER: LISA BARTON

PLAN SPONSOR CONSIDERATIONS

IRS Determination Letter Program

- IRS Revised IRS Determination Letter Program
  - Announcement 2015-19
  - Eliminates staggered five-year remedial amendment cycles for individually designed plans effective January 1, 2017
    - Cycle A plans can continue to submit from February 1, 2016 through January 31, 2017
  - Provides for transition rule for certain plans currently on cycle
  - IRS will no longer accept off-cycle amendments
- Determination letter applications will be permitted for:
  - Initial determinations
  - Terminations
- IRS accepting comments for other situations where a determination letter may be accepted through October 1, 2015

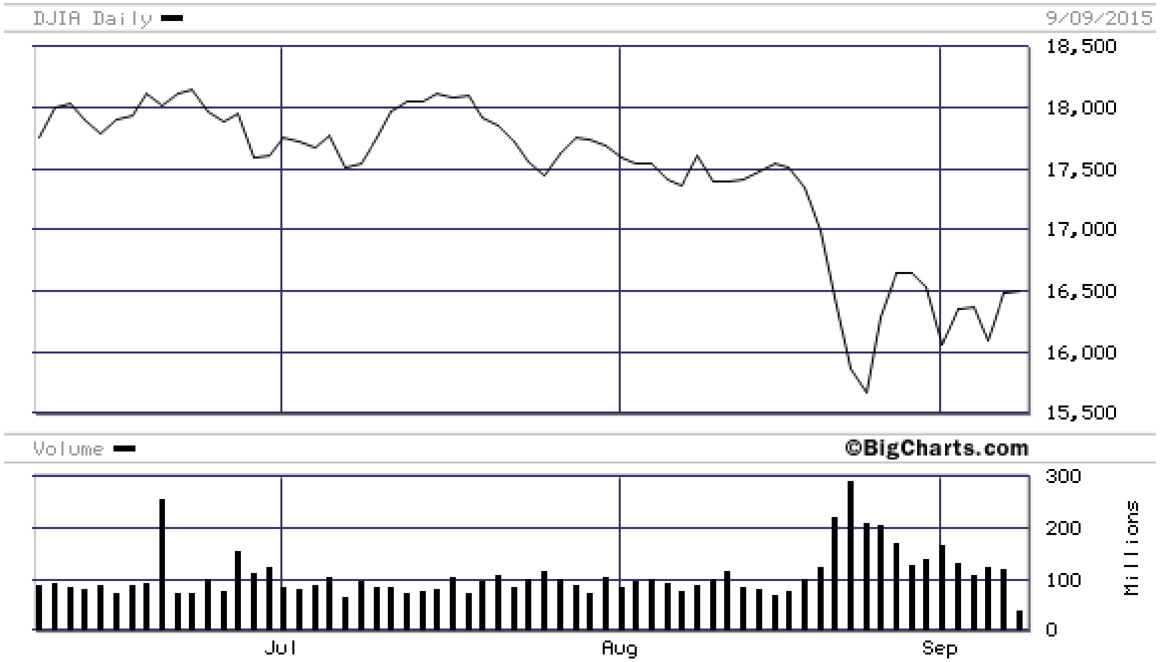
New Guidance on Lump-Sum Windows

- IRS has changed its position on lump-sum windows.
- Previously, plan sponsors may offer lump-sum windows to deferred vested employees and retirees in pay status as part of a "de-risking" plan.
- IRS previously issued private letter rulings (PLRs) that allowed lump-sum amendments to include retirees in pay status.
  - PLRs addressed how a lump-sum window complied with required minimum distribution requirements under Code Section 401(a)(9)
    - Regulations under Code Section 401(a)(9) generally prohibit any change in the period or form of distribution after benefit commencement. In particular, payments must not increase after commencement, except for certain limited exceptions.
- Notice 2015-49 prohibits sponsors of qualified defined benefit plans from adopting lump-sum windows for participants and beneficiaries who are receiving annuity payments due to the fact that they are in pay status.
  - Certain lump-sum window amendments adopted or authorized before July 9 are not affected by the new guidance.

PRESENTER: BRIAN ORTELERE

ERISA LITIGATION

DJIA Last Three Months Say It All



Fifth Third – Supreme Court Backdrop

- Does the Supreme Court's rejection of presumption of prudence in *Fifth Third Bancorp v. Dudenhoeffer* mean a deluge of lawsuits given the recent volatility in the markets?
  - "The same standard of prudence applies to all ERISA fiduciaries, including ESOP fiduciaries, except that an ESOP fiduciary is under no duty to diversify the ESOP's holdings."
  - Moreover, hard wiring not a defense.
  - But opinion arguably circumscribes claims going forward:
    - Claims based upon publicly available information implausible as a general rule, "in the absence of special circumstances," which Court declines to define.
    - Claims based upon inside information problematic given insider trading prohibitions, so claims can go forward only where plaintiff alleges an alternative action "that a prudent fiduciary in the same circumstance would not have viewed as more likely to harm the fund than to help it."

Sampling of Post–*Fifth Third* Rulings

- *Whitley v. British Petroleum* (S.D. Tex., 5th Cir.).
  - Plaintiffs allege that BP stock fund was overvalued in light of alleged undisclosed safety and operational problems that purportedly gave rise to Deepwater Horizon explosion.
  - Plaintiffs allege that fiduciaries could have disclosed inside information about safety deficiencies to the market or stopped further purchases.
  - District court said these issues, the weighing of "relative harm to relative good," might be impossible to determine on the pleadings.
    - Enormous divergence from the court's prior practice, with its emphasis on Rule 12(b)(6).
  - BP argues to Fifth Circuit (second trip to the Court of Appeals, now on interlocutory appeal) that to survive a motion to dismiss, a plaintiff must plausibly allege that a prudent fiduciary could not have concluded that the proposed alternative actions would do more harm than good to the fund.
  - BP filed its brief on August 26, 2015. Stay tuned.

Sampling of Post–*Fifth Third* Rulings

- *Harris v. Amgen* (9th Cir. 2014)
  - District court applied presumption of prudence.
  - CTA9 focused on artificial inflation claim, noting that the profitability and long-term prospects of sponsor irrelevant if stock is in fact artificially inflated.
  - "It is at least plausible that defendants could have removed the Amgen Stock Fund from the list of investment options available to the plans without causing undue harm to plan participants."
  - The insider-trading obstacle is of no moment.
    - "Compliance with ERISA would not have required defendants to violate [securities] laws; indeed, compliance with ERISA would likely have resulted in compliance with the securities laws."
    - And refusing additional purchases would not have run afoul of securities laws because, in that circumstance, "there is no violation absent purchase or sale of stock."
  - Also, fraud-on-the-market theory excuses need to show individual reliance.

Sampling of Post–*Fifth Third* Rulings

- *Gedek v. Perez* (W.D.N.Y. Dec. 17, 2014)
  - Special rule for bankruptcy?
  - “Given these allegations, the fact that the market, on any given date, may have provided the best available estimate on the ‘value’ of company stock, does not necessarily reveal much about whether defendants acted prudently in continuing to invest in that stock.”
  - That said, “*Dudenhoeffer* provides little explicit guidance on [the question] whether plaintiffs have stated a prudence claim.”
  - Finds support in the “dire circumstances” strand of the presumption of prudence.
    - Cites to dissenting opinion in Second Circuit’s ruling.

Sampling of Post–*Fifth Third* Rulings

- *In re RadioShack ERISA Litig.* (N.D. Tex.).
  - Enormously lengthy (108 pages) consolidated amended complaint breathlessly catalogs the slow "inevitable" decline of RadioShack over the last 10 years.
  - Expressly disavows insider information claims. Plaintiffs struggling with *Dudenhoeffer's* pleading standards.
  - Apparently looking to bring within "rule" of *Perez.*
  - Acknowledges impact of public disclosures on RSH stock price, conceded efficient market hypothesis.
  - Plaintiffs blew some toes off?
    - Statute of limitations.
    - The return of ERISA section 404(c)?
      - *EDS* still good law, never overruled en banc.
      - Difficult to imagine, given peculiar allegations regarding publicly available information, better vehicle for the resuscitation of 404(c).

PRESENTER: MIMS MAYNARD ZABRISKIE

EXECUTIVE COMPENSATION

Proposed Dodd-Frank Clawback Rules

- On July 1, 2015 the SEC issued proposed rules under the Dodd-Frank Act relating to clawback policies
- See the PowerPoint from our webcast on July 22, 2015 for more details: http://www.morganlewis.com/events/a-practical-look-at-the-secs-proposed-clawback-rules.

Proposed Dodd-Frank Clawback Rules

- **Clawback Policy** – Listed companies must adopt and disclose a written policy to recoup “incentive-based compensation” in the event of an accounting restatement due to the material noncompliance of the company with any financial reporting requirement under the securities laws (no-fault rule)
- **Incentive-based Compensation** – Any compensation “granted, earned or vested” based wholly or in part on any financial reporting measure
- **Coverage** – Any current or former executive officer who received erroneously awarded incentive-based compensation (including stock-based compensation)
- **Period** – The three completed fiscal years immediately preceding the date on which the company determined or should have determined that a restatement would be required
- **Amount** – The excess over what would have been paid giving effect to the accounting restatement

Proposed Dodd-Frank Clawback Rules

- Recovery is required (not discretionary)
- Listed companies that do not adopt, disclose, and comply with their recovery policies will be subject to delisting from their exchanges
- Applies to smaller reporting companies, emerging growth companies, and foreign private issuers
- Does not apply to companies with securities traded only on OTC market
- Companies will be required to disclose clawback policies and actions taken to recover erroneously awarded executive compensation

Proposed Dodd-Frank Clawback Rules

- Proposed timing for final rule

Action	Timing
Exchanges file proposed listing rules	within 90 days after publication of final SEC rule
Exchanges' rules must be effective	within one year after publication of final SEC rule
Companies must adopt recovery policy	within 60 days after the effective date of the exchange's rules
Companies must recover excess incentive-based compensation resulting from accounting restatement for any fiscal period ending on or after the effective date of the SEC rule	any accounting restatement after the company adopts its policy
Companies must provide disclosures in proxy or information statements and Exchange Act annual reports	for all filings on or after the effective date of the exchange's rules

Proposed Dodd-Frank Clawback Rules

- Issuer required to recover erroneously awarded compensation unless doing so is “impracticable”
  - Recovery required even if there is no misconduct or if the executive officer had no role in preparing a financial statement that is later restated
- Recovery would be “impracticable” only if:
  - The direct expense paid to a third party to assist in enforcing recovery would exceed the amount to be recovered, or
  - Recovery would violate a home-country law adopted before the publication of the final rule (based on an opinion of home-country counsel)
- Before reaching the conclusion that recovery is “impracticable,” a company must first make a reasonable attempt to recover the compensation, document its attempt, and provide the documentation to its exchange

Proposed Dodd-Frank Clawback Rules

- Incentive-based compensation: compensation that is granted, earned, or vested based wholly or in part upon the attainment of a financial reporting measure.
- Financial reporting measures are (1) measures that are determined and presented in accordance with accounting principles used in preparing the issuer's financial statements, (2) measures that are derived wholly or in part from such measures (non-GAAP), (3) stock price, and (4) total shareholder return (TSR).

Proposed Dodd-Frank Clawback Rules

- Incentive-based compensation *does not* include:
  - Awards earned based solely upon the occurrence of nonfinancial events
    - Opening a specified number of stores
    - Obtaining regulatory approval of a product
  - Awards earned upon satisfaction of strategic measures, such as completing a merger, divestiture, or similar transaction
  - Awards that vest solely based on service
  - Salaries
  - Discretionary bonuses
  - Bonuses paid on subjective standards, such as leadership

Proposed Dodd-Frank Clawback Rules

- Incentive-based compensation is deemed to be "received," and therefore recoverable, in the fiscal period when the financial reporting measure is attained
- Actual payment date does not matter

- Recoverable compensation = amount the executive received less the amount the executive would have received had the incentive-based compensation been based on the accounting restatement
- Recoverable compensation is calculated on a *pretax* basis
- Under the Internal Revenue Code (IRC), it is possible for an executive to recoup the taxes previously paid on recovered/clawed-back compensation, through somewhat complicated tax provisions

Proposed Dodd-Frank Clawback Rules

- SEC proposal would prohibit a listed company from indemnifying or purchasing insurance for any executive officer or former executive officer against the loss of any erroneously awarded compensation.
- Executive officers could personally purchase third-party insurance (to the extent such insurance is available) to fund potential recovery obligations.
- Companies would not be permitted to pay, or reimburse the executive officer for, premiums.

Proposed Dodd-Frank Clawback Rules

- Ensure that employment agreements and incentive plans contain provisions to enable implementation of clawback policy.
  - Create a contractual link between the incentive compensation and the recovery policy.
- Consider whether the executive officer scope is appropriately defined.
- Identify financial measures that may cause incentive compensation to become subject to clawback and consider how the recovery process would work for each.
- Consider whether incentive plans should be redesigned to address clawback considerations.
- Consider imposing holding requirements on earned incentive awards.

Proposed Dodd-Frank Clawback Rules

- Review insurance arrangements to determine whether recovery liability is covered by the insurance.
- Review committee charters and other relevant board documents to ensure that the responsibility for determining the Dodd-Frank recovery process is appropriately addressed.

PRESENTER: ALTHEA DAY

MULTIEMPLOYER PLANS

Multiemployer Plans

- Update – ACA Reporting for Employers Contributing to a Multiemployer Plan

- Developments in Successor Liability for Multiemployer Pension Contribution and Withdrawal Liability in Asset Sale Transactions

Update – ACA Reporting for Employers Contributing to a Multiemployer Plan

- Background
- ACA imposes requirements on employers and individuals
  - Employer mandate:
    - Employers must provide affordable, minimum essential coverage to a specified percentage of full-time employees or face a penalty
  - Individual mandate:
    - Individuals must have health insurance or face a penalty
- The IRC requires reporting of information to administer the ACA mandates, and the IRS has issued two sets of forms
  - Section 6055 Reporting (1094/1095-B Forms)
    - To administer the individual mandate
  - Section 6056 Reporting (1094/1095-C Forms)
    - To administer the employer mandate

ACA Reporting for Employers Contributing to a Multiemployer Plan

- Section 6055 Reporting (Forms 1094/1095-B)
  - Requires reporting by any employer that offers minimum essential health coverage (MEC)
  - Report issued to each individual enrolled in MEC, and also to the IRS
    - Reports on MEC coverage for each individual during the year, on a monthly basis
  - Where coverage is provided through a multiemployer health plan, the plan is responsible for this reporting

ACA Reporting for Employers Contributing to a Multiemployer Plan

- Section 6056 Reporting (1094/1095-C Forms)
  - To administer the employer-shared-responsibility mandate
    - Capture individual eligibility for a premium tax credit
  - All applicable large employers (ALEs) must report
  - ALE – 50 full-time or full-time-equivalent employees
    - Employer reporting obligation even if coverage is offered by a multiemployer plan and the multiemployer plan is responsible for the 1094/1095-B reporting
- Section 6056 Reporting (C Forms)
    - All ACA full-time employees are included in the reporting regardless of whether offered MEC
- Challenge – forms require employers to obtain from multiemployer health plans (and plans to provide to employers) specific data about employee coverage
  - Raised COBRA compliance considerations
  - Administratively difficult

ACA Reporting for Employers Contributing to a Multiemployer Plan

- New Guidance – 2015 Draft Directions for Form 1095-C
  - A welcome development for 2015 reporting applicable to employers covered by the multiemployer plan interim guidance
    - Under Code Section 4890H interim guidance, an employer is treated as offering health coverage to an employee if the employer is required by a collective bargaining agreement to make contributions for that employee to a multiemployer plan that offers, to individuals who satisfy the plan's eligibility conditions, health coverage that is affordable and provides minimum value, and that also offers health coverage to those individuals' dependents
- Draft instructions clarify that for 2015 Form 1095-C reporting, employers covered by the multiemployer plan interim guidance need to know:
  - The employees for whom they are required to contribute to a multiemployer plan (this information needs to be captured on a monthly basis)
  - That the multiemployer plan provides minimum essential coverage to employees and dependents up to age 26; and
  - That the coverage is affordable

ACA Reporting for Employers Contributing to a Multiemployer Plan

- For employers covered by the multiemployer plan guidance, to complete the 1095-C Form the employer enters 1H on Line 14 for any month for which the employer enters Code 2E on Line 16 (indicating that the employer was required to contribute to a multiemployer plan on behalf of the employee).
- This guidance greatly simplifies the amount of information that needs to be exchanged between a multiemployer plan and the contributing employer.
- Only for 2015 – the IRS has indicated that for 2016 and later years, coverage through a multiemployer plan may be reported by a different method.

ACA Reporting for Employers Contributing to a Multiemployer Plan

- ACA reporting deadlines – Forms 1094/1095-B and -C
  - IRS filing deadline is March 31 (if filed electronically—requires 250 or more individual Forms 1095-C)
    - February 28 if not filing electronically
    - Automatic 30-day extension for IRS filing; must apply before otherwise applicable due date; may not file for extension prior to January 1 of the filing year (e.g., February 1, 2016 for 2015 reporting)
  - Reports to individuals due January 31
    - IRS may grant an extension of up to 30 days
    - Need to apply by letter before due date for filing and include the reason for the extension
    - Extension not automatic

Developments in Successor Liability for Multiemployer Pension Contributions and Withdrawal Liability in Asset Sale Transactions

- General rule under common law is that where a company purchases assets of another company, the purchaser is not automatically responsible for the seller’s liability unless:
  - the purchaser expressly or impliedly assumes such liability through the purchase agreement or
  - the transaction constitutes a de facto merger (i.e., a continuation of the seller’s business)
- However, a recent trend is developing with courts finding asset purchasers to be “successors” for the seller’s multiemployer pension plan liability

Developments in Successor Liability for Multiemployer Pension Contributions and Withdrawal Liability in Asset Sale Transactions

- Expanded successor liability:
  - *Upholsterers' International Union Pension Fund v. Artistic Furniture* (7th Cir. 1990)
    - United States Court of Appeals for the Seventh Circuit borrowed from federal labor law and held that a purchaser of assets could be liable under ERISA for delinquent pension contributions owed by the seller to a multiemployer pension plan, provided there was sufficient evidence of continuity of operations, and the purchaser knew of the seller's liability
  - *Einhorn v. M.L. Ruberton* (3d Cir. 2011)
    - United States Court of Appeals for the Third Circuit held that a purchaser of assets from a seller obligated to contribute to a multiemployer plan may be liable for the seller's delinquent contributions where there was a continuity of operations and the purchaser knew of the delinquency

Developments in Successor Liability for Multiemployer Pension Contributions and Withdrawal Liability in Asset Sale Transactions

- *Tsareff v. ManWeb Services, Inc.* (7th Cir. 2015)
  - United States Court of Appeals for the Seventh Circuit took an additional step to expand potential successor liability, holding that an asset purchaser could be liable for the seller's withdrawal liability triggered as a result of an asset sale, provided that the purchaser had known that the seller's "contingent" multiemployer pension withdrawal liability would be triggered by the sale.
    - The United States District Court for the Southern District of Indiana originally found that the seller in *ManWeb* was liable for the withdrawal liability because it failed to initiate required arbitration contesting the withdrawal liability assessment, and that the purchaser was not liable as a successor because it did not have proper notice of the claim prior to the asset sale.
    - The seller did not withdraw from the pension plan until after the sale, and the district court found the purchaser's preacquisition notice of a contingent pension liability to not be sufficient. The multiemployer pension plan sued both the seller and the purchaser in the transaction for the payment of the withdrawal liability with the claim against the purchaser based on the theory of successor liability.

Developments in Successor Liability for Multiemployer Pension Contributions and Withdrawal Liability in Asset Sale Transactions

- *Tsareff v. ManWeb Services, Inc.* – broadened potential successor liability:
  - The Seventh Circuit found that the buyer knew of the potential withdrawal liability because it engaged in due diligence, was familiar with the concept of withdrawal liability, and addressed benefit plan liability in the asset purchase agreement
  - Court also found that the buyer could not challenge the underlying withdrawal liability assessment because the seller waived its right to arbitrate
  - Matter remanded to district court to determine if there was sufficient continuity of operations after the sale for the buyer to be a successor and hence liable

Developments in Successor Liability for Multiemployer Pension Contributions and Withdrawal Liability in Asset Sale Transactions

- *Resilient Floor Covering Pension Trust Fund Board of Trustees v. Michael's Floor Covering* (9th Cir. 2015)
  - United States Court of Appeals for the Ninth Circuit has for the first time adopted successor liability as a means to hold companies responsible for multiemployer withdrawal liability
    - The Ninth Circuit had previously applied successor liability in other labor and employment contexts, including liability for delinquent multiemployer plan contributions.
    - In *Michael's Floor* the court found that in general a successor employer may be subject to multiemployer pension plan withdrawal liability and, in particular, a construction industry successor employer can be subject to such liability, so long as the successor took over the business with notice of the liability.
    - The court held that the most important factor in assessing whether an employer is a successor for purposes of imposing such withdrawal liability is whether there is substantial continuity in the business operations between the predecessor and the successor, as determined in large part by whether the new employer has taken over the economically critical bulk of the prior employer's customer base.

Asset Sales Considerations

- Given recent case law developments, would-be asset purchasers may want to think carefully about how to structure transactions where the seller has contingent multiemployer pension plan withdrawal liability, especially in the Third and Seventh Circuits
  - Consider structuring under ERISA Section 4204
  - Indemnification or purchase price adjustments

Morgan Lewis

QUESTIONS?

Register for the next webinar in this series:
December 16, 2015

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