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HOT TOPICS IN EMPLOYEE BENEFITS: WHAT WE'RE SEEING

Presenters: Craig Bitman (moderator and presenter), Andy Anderson, Lisa Barton, David Fuller, Jason Ray, and Mims Zabriskie

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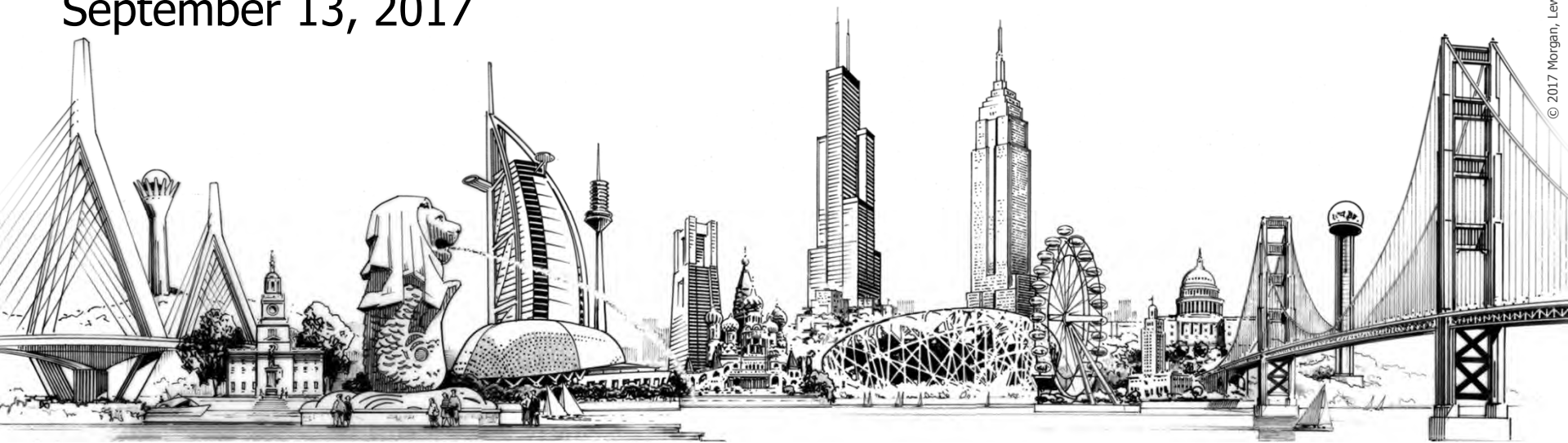

Agenda

- Fringe Benefits
- Health and Welfare
- Executive Compensation Priorities
- Fiduciary Considerations
- Plan Sponsor Considerations
- Employee Stock Ownership Plans (ESOPs)

PRESENTER: DAVID FULLER

FRINGE BENEFITS

Disaster Assistance to Hurricane Victims

Employer Tax-Favored Programs to Assist Hurricane Victims

- Charitable Leave Donation Programs
- Disaster Assistance Leave Banks
- Qualified Disaster Relief Programs
- Employer-Sponsored Charitable Organizations

Disaster Assistance to Hurricane Victims

Charitable Leave Donation Programs

- IRS Notice 2017-48
  - Relief for those affected by Hurricane Harvey
  - Employees can donate the cash value of accrued leave through the employer to charities assisting hurricane victims
  - The three basic requirements
    1. The donations must be made to a Code Section 170(c) organization
    2. The donations are to assist the victims of Hurricane Harvey
    3. The donations must be made prior to January 1, 2019

Disaster Assistance to Hurricane Victims

Charitable Leave Donation Programs

- Tax-Favored Treatment—IRS' Nonenforcement Position
  - Employees—Employees effectively make the donation to the charity on a pre-tax basis (the donation is exempt from income taxes and FICA taxes and available to nonitemizers)
  - Employers—Employers make the actual donation to the charity
    - The donation is exempt from FICA taxes
    - The employer can choose to claim a charitable donation or a business expense
  - The Charity—the donations are larger than if the employee had received and then donated the leave to the charity

Disaster Assistance to Hurricane Victims

Disaster Assistance Leave Banks

- Employees donate leave to affected co-workers who will exhaust their own leave due to Hurricane Harvey
- Unlike charitable leave donation programs, these programs can be used when a broader array of disasters
- IRS Notice 2006-59 authorizes the program
  - Similar to medical assistance leave banks under Rev. Rul. 90-29, except targeted toward disaster assistance relief

Disaster Assistance to Hurricane Victims

Disaster Assistance Leave Banks

- Tax Treatment
  - The employee donating the leave is not taxed on the leave donation
  - The co-worker receiving the leave is taxed at his or her wage rate when in actual receipt of the paid leave
- Considerations
  - The leave bank can accept and distribute leave on a disaster-by-disaster basis but carryovers to future disasters are not permitted
  - Leave in the bank at the end of the disaster should be reallocated

Disaster Assistance to Hurricane Victims

Qualified Disaster Relief Program

- Employer payments to affected individuals including employees
- Code Section 139 allows an employer to directly assist employees who are adversely impacted by a "qualified disaster"—not just disasters of the magnitude of Hurricanes Harvey and Irma
- The employer makes payments to or for the benefit of an "individual" (not just an employee):
  - To pay or reimburse reasonable and necessary personal, family, living or funeral expenses or expenses for home repair
  - The expenses must not be reimbursable by insurance "or otherwise"

Disaster Assistance to Hurricane Victims

Qualified Disaster Relief Program

- Favorable Tax Treatment
  - The payments are not taxable as wages to the recipient
  - The employer claims a Section 162 business deduction for the payments
- The program does not need to be a written program or policy, but employers should consider:
  - Adopting a written policy limiting the use of funds
  - Requiring a simple statement from the employee as to the use of the funds and that the expenses are not otherwise reimbursable

Disaster Assistance to Hurricane Victims

Employer-Sponsored Charitable Organizations

- Employer-Sponsored Public Charity
- Employer-Sponsored Donor-Advised Funds
- Employer-Sponsored Private Foundations

PRESENTER: ANDY ANDERSON

HEALTH AND WELFARE

THE AFFORDABLE CARE ACT—WHAT COMES NEXT?

Repeal and Replace—Senate (In) Action

- ACA "Perils of Pauline" continue unabated
- Apparently dead (for now), as Senate failed to pass any Repeal and Replace legislation, including the American Health Care Act of 2017 (AHCA), and a "Skinny Repeal" bill based on successful--and vetoed--Obama-era legislation
  - Dramatic late night vote July 27
  - Republican Senate dissenters:
    - Murkowski
    - Collins
    - McCain
- Difficult failure to deliver on Republican campaign promises
- Sweeping ACA reforms, and Medicaid revisions, seem beyond reach

Repeal and Replace—House Bill

- What Affordable Care Act (ACA) provisions would have stayed?
- Only addressed ACA provisions that have a federal budget impact
  - Federal and state based Exchanges (ACA reporting)
  - Preventive care services with no cost sharing
  - Dependent coverage to age 26
  - Appeals and external review standards
  - Provider nondiscrimination rules
  - Prohibition of lifetime and annual dollar limits
  - Essential health benefits standards (subject to state waivers)
  - Prohibition on pre-existing condition exclusions

Repeal and Replace—House Bill

- What ACA provisions were to stay?
  - Requirement for all plans to apply in-network level of cost sharing for out-of-network emergency services is not changed
  - SBCs
  - Wellness incentives permitted under ACA

2017 Planning—No Changes

- No legislation will impact 2017 calendar year ACA rules in the employer market

2018 Changes—Unlikely

- Retention of current ACA employer regime
  - Do not expect any meaningful legislation to impact 2018 calendar year ACA rules in the employer market
  - Any Individual Market reforms may have knock-on impact for employers
- Health Insurance Tax returns from a one-year moratorium

What Happens Next?

- Limited "Fix" legislation
  - Focused on individual market support
  - Series of unsatisfactory think tank proposals have surfaced/resurfaced
    - Some jeopardize the employer deduction for healthcare costs
- Regulatory Rollback
  - Postpone enforcement
  - Expanded State waivers (and associated ERISA preemption worries)
  - Regulators collected input on rollback ideas
- Continuing Cost Sharing subsidies drama
- Broad bipartisan ACA "fix" will not occur
- Tax Reform may address Cadillac Tax and employer deduction
- Meaningful legislation may await 2018 midterm election results

PRESENTER: MIMS ZABRISKIE

EXECUTIVE COMPENSATION PRIORITIES

EXECUTIVE COMPENSATION PRIORITIES

- Preparations for CEO pay ratio disclosure should be underway.
  - Start early on proxy disclosure.
  - Plan how to manage the message to company employees.
- Check equity plans and bonus plans to determine whether shareholder reapproval is necessary.
  - Section 162(m) generally requires shareholder approval every five years for plans that authorize grants of "performance-based compensation."
  - Start the process early. ISS and other shareholder considerations make the process more time consuming than in the past.
  - See our blog on equity plan approval at https://www.morganlewis.com/blogs/mlbenebits.

EXECUTIVE COMPENSATION PRIORITIES

- Review performance metrics and goals used for 2017 grants to determine whether changes should be made for 2018 grants and annual bonus plan
  - ISS is scrutinizing performance goals to make sure they are rigorous, and ISS is comparing current year goals to prior year goals
- Review your peer group for appropriate changes

EXECUTIVE COMPENSATION PRIORITIES

- Fall is usually the best time for shareholder outreach
  - Plan outreach thoughtfully: who should attend; clear communication of important points; compliance with SEC rules
  - Create a record of Compensation Committee consideration of viewpoints expressed by shareholders in the outreach process

- Consider whether to allow increased share withholding for taxes on equity awards
  - See our blog outlining issues to be considered at https://www.morganlewis.com/blogs/mlbenebits.

EXECUTIVE COMPENSATION PRIORITIES

- Nonqualified deferred compensation plans
  - Review compliance with Section 409A. Corrections of errors are significantly easier to make if they are caught early.
  - Ensure that "top hat" plans are continuing to be limited to a select group of management or highly compensated employees.

PRESENTER: CRAIG BITMAN

FIDUCIARY CONSIDERATIONS

Update on Status of the Fiduciary Rule

- Brief Background
  - The Department of Labor (DOL) has revised a 33-year-old regulation defining when a person is considered a fiduciary when providing investment advice.
  - The overall effect of the rule will be to broaden the investment advice that is considered fiduciary and the parties who will be considered fiduciaries.
  - There have been many twists and turns in the path to the rule's applicability, including as a result of the new administration.
  - The rule became final on June 6, 2016 and was slated to become "applicable" on April 10, 2017. That date was delayed 60 days until June 9, 2017.
  - Two new prohibited transaction exemptions were adopted along with the rule—one called the Best Interest Contract Exemption and one called the Principal Transaction Exemption. Several provisions of these exemptions do not become applicable until January 1, 2018.

Update on Status of the Fiduciary Rule

- Most Recent Developments
  - On April 7, 2017, the DOL issued a notice delaying the applicability date by 60 days (until June 9, 2017).
    - Notice was issued on the last business day before the originally proposed applicability date
    - Loosened some of the exemption conditions
    - But "impartial conduct standards" become applicable on June 9

Update on Status of the Fiduciary Rule

- Most Recent Developments
  - On May 22, 2017, the DOL issued Frequently Asked Questions (FAQs) regarding the transition period between June 9, 2017 and January 1, 2018.
    - On July 6, 2017, the DOL issued a Request for Information for "additional public input on specific ideas for possible new exemptions or regulatory changes based on recent public comments and market developments."
      - Specifically mentioned further consideration of "clean shares"
      - Possibility of streamlined requirements for certain types of products
  - The DOL reiterated that there will be no regulatory enforcement until at least January 1, 2018 for those working diligently and in good faith to comply with the impartial conduct standards.
  - On August 31, 2017, the DOL issued a proposed rule to delay the applicability of the additional aspects of the BIC Exemption and other exemptions until July 1, 2019.
  - On the same date, the DOL also issued a Field Assistance Bulletin providing for a nonenforcement policy with respect to the BIC Exemption's and other exemptions' prohibitions on class action waivers and qualifications.

Update on Status of the Fiduciary Rule

- What's Next?
  - Financial service provider clients are generally attempting to comply in good faith as of June 9 with the impartial contract standards – for those relying on the BIC Exemption
  - Plan sponsor clients should confirm how participant-facing service providers intend to comply with the rule
    - Advice vs. education
    - Rollovers
  - Plan sponsors are also receiving various types of communications about the so-called "independent fiduciary exclusion"
    - Special rule for communications to sophisticated fiduciaries independent of the party providing the communication
    - Requires the party providing the communication to confirm that certain conditions are met
    - Plan sponsors may be asked to make affirmative representations or deemed representations via "negative consent"
    - Take care that the representations don't go too far
  - As always, stay tuned. This isn't over.

PRESENTER: LISA BARTON

PLAN SPONSOR CONSIDERATIONS

Department of Labor Audits

- Department of Labor (DOL) Auditing Defined Benefit Plans
- Audits relate to
  - Timely processing required for minimum distributions
  - Location of missing participants
  - Reconciliation of census data
- Audits have been mainly in the East (Philadelphia, New York, and New Jersey DOL offices)
- Plan fiduciaries should
  - Determine procedures for processing required minimum distributions
  - Confirm if RMDs have been timely processed
  - Verify procedures for locating missing participants
  - Confirm if census data can be properly reconciled

PRESENTER: JASON RAY

EMPLOYEE STOCK OWNERSHIP PLANS (ESOPS)

PTE 80-26 LOANS

- The decision to redeem, recycle or releverage shares from terminated participants' accounts under an ESOP can have a significant effect on future participants' benefit levels, stock price and repurchase liability.
- If the decision is made to redeem shares from the ESOP, an updated valuation will usually be required if shares are not distributed to participants with a put option (or automatic put) back to the company. This updated valuation can be costly in both time required to supply updated information to the valuation firm and additional fees for the update. If the new stock price is different from the last annual valuation, there can be additional administrative and participant communication issues.
- In order to convert terminated participants' account balances within the ESOP, it may make sense for the plan sponsor to loan money to the plan, but the Internal Revenue Code prohibits certain transactions between employee benefit plans and "parties in interest." These prohibited transactions include the "lending of money or other extension of credit between the plan and a party in interest."

PTE 80-26 LOANS (Cont.)

- Many ESOP sponsors rely on a Prohibited Transaction Exception (PTE) 80-26 loan.
- PTE 80-26 allows for interest free loans from an employer to a plan.
- The key is complying with PTE 80-26's requirements:
- No interest or fee is charged to the plan for the loan from the employer.
- The plan does not waive any discount for payment in cash.
- Loan proceeds must be used for:
  - Payment of ordinary plan operating expenses
  - For a purpose incidental to the operation of a plan
- The loan is unsecured
- The loan is not directly or indirectly made by a plan
- The loan is not an ESOP acquisition loan
- Loans for more than 60 days must be written and describe material terms

PTE 80-26 LOANS (Cont.)

If a PTE 80-26 loan is used to make distributions or convert terminated participants' accounts, the loan can be repaid as of the next annual valuation date.

- One option for the repayment of the loan would be to redeem the number of shares equal in value to the loan amount at the new share price.
- If the share price has increased since the last valuation, there will be additional shares, which can be allocated to participants as earnings.
- If the share price has decreased, only the number of shares that were converted would be redeemed.
- Shares redeemed from the trust could then be retired by the plan sponsor, contributed back to the plan or sold to the trust in a leveraged transaction, if desired.

Biography

Andy Anderson
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Leader of Morgan Lewis's health and welfare task force, Andy R. Anderson is often recognized for his work in counseling clients on employer, individual, and insurer issues created by the Affordable Care Act, and regulatory compliance issues in relation to the Internal Revenue Code, ERISA, COBRA, HIPAA, and Mental Health Parity. Tax-exempt organizations and Fortune 500 companies turn to Andy for handling their benefit plans, and legal review surrounding welfare benefit plans, government self-correction programs, cafeteria plans, and VEBAs.

Biography

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Craig A. Bitman provides clients with a range of knowledge and skills in all aspects of employee benefits and executive compensation law. He not only serves as deputy practice leader, but also as leader of the practice's Fiduciary Task Force and co-chair of the firm's institutional investor practice. Craig also practices in the firm's private investment funds practice and is a member of the firm's Advisory Board.

Biography

Lisa Barton
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Lisa H. Barton advises clients in designing, drafting, and operating tax-qualified retirement and health and welfare plans, as well as nonqualified deferred compensation and equity compensation plans. She counsels companies on complying with the US Internal Revenue Code, ERISA, COBRA, the Affordable Care Act, and other state and federal laws pertaining to benefit plans and programs. Her clients come from such industries as retail, manufacturing, life sciences, energy, and information technology.

Biography

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David R. Fuller advises Fortune 500 clients on tax planning and controversy matters involving employment taxes, fringe benefits, and contingent workforce issues. He helps enterprises address matters related to payroll taxes, including worker classification involving Social Security taxes, and Section 530 relief and Section 3121(v) of the Internal Revenue Code. He also advises on matters involving independent contractors, income tax withholding, supplemental unemployment compensation benefit plans (SUB pay), employee outsourcing, and information reporting.

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Jason C. Ray advises employers on the design, implementation, and regulatory compliance of tax-qualified and nonqualified retirement plans. In addition to counseling clients on all aspects of employee benefits, Jason appears before the IRS and the US Department of Labor to review penalty assessments, plan correction, and plan audit, among other benefits matters. Jason guides clients in employee stock ownership plan (ESOP) transactions, including seller-financed and leveraged and nonleveraged buyouts as part of ownership succession transactions.

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Mims Maynard Zabriskie advises on complex executive compensation and employee benefit plan matters, including the design, negotiation, and implementation of executive compensation, equity compensation, and tax–qualified retirement plans and shareholder approval of equity plans. She counsels large publicly and privately owned businesses, including Fortune 500 enterprises, technology companies, and universities on a range of legal issues related to executive compensation governance, and employee benefit plans. She also advises on benefits and executive compensation issues that arise during major corporate transactions, including mergers and acquisitions, sales, IPOs, and spinoffs.

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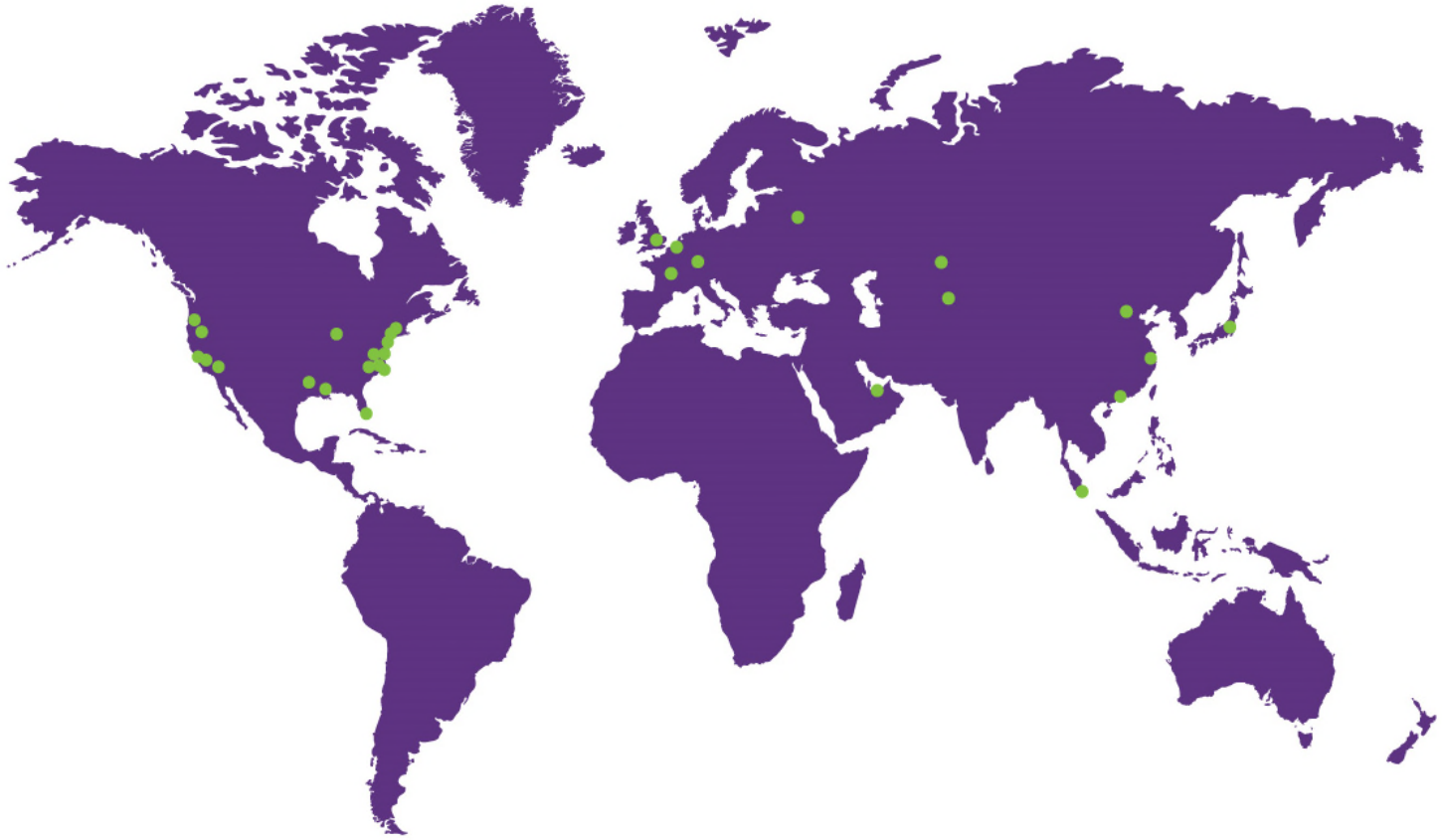

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