Hodgson Russ LLP
ATTORNEYS

EMPLOYEE BENEFITS DEVELOPMENTS
DECEMBER 2013

Hodgson Russ Newsletter
December 20, 2013

Practices & Industries

Employee Benefits

RULINGS, OPINIONS, ETC.

Modification of "Use-or-Lose" Rule for Health FSAs

Internal Revenue Service (IRS) Notice 2013-71 modifies the "use-it-or-lose-it" rule for health flexible spending accounts (health FSAs) set forth under Section 125 of the Internal Revenue Code. Under prior guidance, a Section 125 cafeteria plan generally could not provide for deferred compensation. As such, participants were generally prohibited from using contributions made during one plan year to reimburse expenses incurred in a subsequent plan year. Commonly referred to as the use-it-or-lose-it rule, this required that unused amounts be forfeited at the end of the plan year. In 2005, the IRS modified the use-it-or-lose-it rule by allowing plan sponsors to adopt a grace period. Under the grace period rule, a cafeteria plan may permit a participant to use amounts remaining from the previous year (including amounts from a health FSA) to reimburse expenses incurred for certain qualified benefits during a period of up to two months and 15 days immediately following the end of the plan year. The newest modification of the use-it-or-lose-it rule permits cafeteria plans to be amended to allow up to $500 of unused amounts remaining at the end of a plan year to reimburse qualified medical expenses incurred during the following plan year. However, the cafeteria plan may not also incorporate the grace period rule. For those plan sponsors choosing to include the $500 "carryover" rule, the cafeteria plan must be amended in writing on or before the last day of the plan year from which amounts may be carried over. The amendment may be effective retroactively to the first day of that plan year, provided that the cafeteria plan operates in accordance with the IRS guidance in the notice and informs participants of the carryover provision. The notice also provides that a cafeteria plan may be amended to adopt the carryover provision for a plan year that began in 2013 at any time on or before the last day of the plan year that begins in 2014. In light of this new guidance, plan sponsors should review their cafeteria plans and consider whether this carryover provision fits with their overall benefit strategy.

CASES

Women's Preventive Services and For-Profit Employers

The Affordable Care Act (ACA) requires non-grandfathered group health plans to cover certain preventive health services without cost-sharing. For women, this coverage includes well visits, gestational diabetes screening, testing and counseling for certain sexually transmitted diseases, and breastfeeding support, supplies, and counseling. The regulation also requires plans to cover the full range of contraceptive methods approved the Food and Drug Administration. The contraceptive-coverage requirement includes coverage for drugs and devices (e.g., Plan B, Ella, and two intrauterine devices) that many religious employers contend they cannot cover without violating their faith.

As we discussed in last month's newsletter, "religious employers" (i.e., houses of worship) are fully exempted from the contraceptive requirement. Nonprofit religious organizations that qualify as "eligible organizations (e.g., faith-based schools, nursing homes, and hospitals) may self-certify and route contraceptive payments through their insurer or third-party administrator. The regulations do not exempt or accommodate for-profit employers, regardless of the beliefs held by their owners.

In June 2013, the U.S. Court of Appeals for the Tenth Circuit held that two for-profit companies—Hobby Lobby, Inc. and Mardel, Inc.—and their owners who run their businesses in ways that reflect their religious values are entitled to challenge the women's contraceptive mandate on religious grounds. Hobby Lobby is a chain of more than 500 arts and craft stores that has approximately 13,000 full-time employees across the country. Mardel is a chain of 35 stores selling books and educational supplies and specializing in Christian materials. The owners of these two for-profit corporations filed suit, contending that the requirement that the Hobby Lobby group health plan cover all forms of FDA-approved contraceptives violates the Religious Freedom Restoration Act of 1993 (RFRA), which provides that the government may not substantially burden a person's exercise of religion unless that burden is the least restrictive means to further a compelling government interest. Following the Court's decision, the Departments of Health and Human Services, Labor, and Treasury petitioned the U.S. Supreme Court for a ruling on whether the RFRA allows a for-profit corporation to exclude women's contraceptive services from its medical plan, based on the religious objections of the owners of the corporations.

The Supreme Court has agreed to hear the case. Arguments are planned for early 2014, with a decision possibly as early as June 2014. The Supreme Court's ruling will have major implications for women's rights, the limits of corporate personhood, the "religious expression" of the owners of for-profit companies, and, last but not least, the president's signature health care reform effort.

A Lesson on Maintaining Historical Plan Documents

Robert Hartman worked for Weatherhead for nearly a quarter century before his retirement in 1976. As an employee of Weatherhead, Hartman was a participant in the Weatherhead Pension Plan for Salaried Employees. In 1979, Weatherhead was purchased by Dana Corporation. A subsidiary of Dana became plan sponsor and plan administrator of the plan.

In March 1979, an early commencement request was sent to Hartman with instructions that he sign and return the enclosed election form. The election form provided that Hartman understood he was to receive a single life annuity. Hartman signed and returned the request. Notwithstanding this election, Hartman's wife understood that he had elected a joint and survivor annuity, and she maintained that she never executed a spousal waiver. Indeed, the default payment method for a married participant under the plan was a 50 percent joint and survivor annuity. Following Mr. Hartman's death in April 2011, Mrs. Hartman contacted Dana to inquire into her rights to a survivor annuity.

Over the next year, Mrs. Hartman and her attorney made numerous requests for Mr. Hartman's election form, a spousal waiver form, and the 1979 plan document and summary plan description (SPD), although a written request to Dana was not made until May 2012 as part of a claims appeal letter. On June 6, 2012, Dana provided Mr. Hartman's election form. No other documents were provided at that time. After being advised that Dana considered the election form to resolve the issue, Mrs. Hartman filed suit against the company for its failure to provide the documents she requested, among other claims. Although Dana eventually produced the SPD in effect during May 1979, the SPD did not answer the question of whether a spousal consent was required for a married participant to elect a form of benefit other than the 50 percent joint and survivor annuity.

Section 502 of the Employee Retirement Income Security Act of 1974 (ERISA) creates a cause of action under which participants and beneficiaries (a beneficiary includes a person who may become entitled to benefits under the plan) may bring suit for a plan administrator's failure to provide documents under which the plan is established or operated within 30 days of a participant or beneficiary's written request for those documents. A noncompliant plan administrator may be held liable for up to $110 per day for failing to produce the requested documentation within the required 30 days.

As a threshold matter, the court found Mrs. Hartman to be a "beneficiary" at the time she filed suit because it was unclear whether her consent was required for Mr. Hartman to elect a single life annuity; the fact that the SPD made no mention of a spousal consent requirement was irrelevant for purposes of establishing Mrs. Hartman's status as a beneficiary. The court then found that Dana was obligated by ERISA to provide the historical plan document and SPD to Mrs. Hartman because they contained information necessary for her to understand and assert her rights under the plan. As a result, the court imposed a penalty of $10 per day, ending on the date the relevant SPD was provided to Mrs. Hartman, resulting in an aggregate penalty amount of $4,470. The lower fee (i.e., $10 per day instead of $110), reflected the facts that there was no evidence of bad faith by Dana and that Mrs. Hartman was not actually harmed.

While the statutory penalty in this instance might be described as relatively nominal, the importance of maintaining historical plan documents cannot be understated. In addition to the potential for statutory penalties for the failure to provide requested plan documents, missing historical plan documentation potentially makes defending claims for benefits and assertions of a breach of fiduciary duty under ERISA more difficult to defend. Issues could also arise with respect to a plan's qualified tax status. At the same time that more and more employers are shifting toward pre-approved plan documents, the IRS has announced that it generally will no longer review a determination letter application with respect to an ongoing pre-approved plan because it would have already reviewed the form of the plan document submitted by the document provider. However, in our experience, when an employer applies for an IRS determination letter on plan termination, or when the IRS reviews a determination letter application for a plan into which a pre-approved plan has been merged, the IRS requests all plan documents in effect since the terminating or merged plan last received an IRS determination letter. In the case of a pre-approved plan that has never received a determination letter, this can prove difficult.

To guard against potential issues related to missing historical documentation, a number of steps are recommended: (1) plan officials should carefully review services agreements with plan service providers to analyze what the agreement says about document retention, both during the period the service provider is retained and at termination of those services and (2) in the context of corporate transactions, if the employee handling benefits at the target company is to be terminated following the closing, the surviving company should make sure it knows the status and location of the target company's benefits records before the employee leaves – or, in a perfect world, make sure it has received all historical plan documents during the course of its due diligence. (*Hartman v. Dana Holding Corp*., N.D. Ind., 2013)

First Spouse Awarded Survivor Pension Benefits

From November 1978 through December 1991, an employee was covered by a pension fund. He married his first spouse in 1979, and the couple appear to have *never* divorced. The employee married his second spouse in a different state in 1995. In 1997, the employee retired and applied for benefits from the pension fund. On his pension application, the employee identified himself as married and named his second spouse as his spouse for purposes of a "50 percent husband–and–wife" benefit option he elected. The employee attached to his benefit application a copy of his marriage certificate memorializing his marriage to the second spouse. Following the employee's death in January 2007, the pension fund began paying the second spouse a monthly survivor pension on February 1, 2007. The employee's first spouse applied for survivor benefits from the pension fund later in February 2007, attaching her 1979 marriage certificate and explaining that she and the employee had never divorced.

An interpleader action was commenced, and the Eastern District of Tennessee concluded the second spouse was the proper beneficiary of the employee's pension benefits. Reasoning that the employee's pension plan documents supply the exclusive basis for settling a beneficiary dispute, the district court concluded the second spouse was entitled to survivor benefits because the employee identified the second spouse as both his spouse and his beneficiary in his pension application.

The first spouse appealed the district court decision, and the Sixth Circuit Court of Appeals reversed the district court's decision, essentially holding that a plan administrator must follow plan terms to determine the proper beneficiary. The terms of the pension fund guaranteed the employee's spouse a survivor pension starting after his death unless the spouse consented in writing to waive the survivor benefit, and the plan documents define "spouse" as "a person to whom a participant is legally married." The Sixth Circuit held that no finding had been made at the district court level as to whether the marriage between the employee and his first spouse was legally dissolved prior to his marriage to his second spouse, and thus no finding had been made as to whether the employee and his second spouse were legally married at the time of his death. Because the plan must pay survivor benefits to the employee's legal spouse to comply with the terms of the pension fund, the Sixth Circuit remanded the case to the district court to determine which spouse was the employee's legal spouse at the time of death.

On remand, the district court relied on Tennessee law and found there is a presumption favoring the validity of the employee's second marriage. Under that presumption, the employee's marriage to his first spouse was presumed to have been dissolved by divorce when he married his second spouse. To attack the validity of the second marriage, the first spouse has the burden of overcoming the presumption by clear and convincing evidence. Based on the evidence presented, however, the district court found that the first spouse indeed was able to provide sufficient evidence to overcome the presumption favoring the validity of the second marriage. Among other things, the district court found it significant that the first spouse not only had knowledge of the pension fund but knew she would be entitled to survivor benefits as the employee's spouse. Had a divorce occurred, the first spouse would have sought payment of a portion of the pension fund (presumably via a qualified domestic relations order) at the time of the divorce; her decision to wait to seek a portion of the pension benefit until after the employee's death adds credibility to her assertion that there had never been a divorce. Accordingly, the first spouse was determined to be the legal spouse at the time of the employee's death. And because the first spouse never waived her spousal rights, she is the proper beneficiary under the pension fund. (*IBEW Pacific Coast Pension Fund v. Lee*, E.D. Tenn., 2013)

Claim for Post-Bankruptcy Pension Benefits Rejected Following "Free and Clear" Purchase of Assets

A group of retired employees filed a class-action law suit claiming loss of certain retirement benefits. The employees worked for SPX Corporation until 1996 when it was acquired by Dana Corporation. SPX sponsored a pension plan for these employees. In 2006, Dana filed a Chapter 11 bankruptcy and sold certain assets to Mahle gmbH. Under the asset purchase agreement, Mahle assumed certain benefit plans. The dispute arises over eligibility for supplemental retirement benefits under a plan Mahle assumed from Dana. The SPX pension plan had a supplemental retirement feature that was conditioned on completing 30 years of service or attaining a certain combined age and service of 85. The plan Mahle assumed counted all service with SPX and Dana for eligibility but only counted service with Dana for benefit accrual. The group of retired employees do not qualify for a supplemental retirement feature under the plan Mahle assumed. The retirees filed this action claiming that Mahle assumed "pension obligations" of Dana, including the supplemental retirement feature provided in the SPX plan. The District Court for the Western District of Michigan granted summary judgment, rejecting the retirees' complaint. The court found that the Mahle bought the assets "free and clear" from the bankruptcy estate and that the pension obligation being claimed by the retirees was not a liability that was assumed by Mahle. The court found the free and clear sale provisions under the Bankruptcy Code means that Mahle purchased assets from Dana free and clear, and unless such claim was expressly assumed by purchaser, which Mahle did not do, the obligation to provide supplemental retirement benefits did not carry over to Mahle as a successor. (*Auto Workers v. Mahle Engine Components USA, Inc.*, W.D. Mich., 2013)

Employee Benefits Practice Group

Peter K. Bradley pbradley@hodgsonruss.com
Anita Costello Greer agreer@hodgsonruss.com
Michael J. Flanagan mflanagan@hodgsonruss.com

Richard W. Kaiser rkaiser@hodgsonruss.com
Arthur A. Marrapese, III art_marrapese@hodgsonruss.com
Ryan M. Murphy rmurphy@hodgsonruss.com