EMPLOYEE BENEFITS DEVELOPMENTS SEPTEMBER 2013

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Employee Benefits

RULINGS, OPINIONS, ETC.

Play or Pay Penalties Postponed

In a well-publicized release, formalized in IRS Notice 2013-45, the Obama Administration announced that no "play-or-pay" penalties would be assessed for 2014. This was welcome news for many employers, and most then turned their attention to more pressing matters, including certain Affordable Care Act provisions that were not postponed. These provisions include the summary of benefits and coverage requirement; the new 90-day limit on waiting periods; the new maximum limits on deductibles and out-of-pocket expenses; compliance with the new wellness plan regulations impacting, in particular, outcome-based reward programs; and, last but not least, the Marketplace Exchange Notice that is due October 1, 2013. While the delay does provide some breathing room, sponsors of calendar year plans (and perhaps non-calendar year plans) that will use 11- or 12- month measurement periods for variable hour and seasonal employees will need to start counting hours for payroll periods that begin in October 2013. The IRS did not address non-calendar year plans in Notice 2013-45, and it is not clear when the penalties apply to these plans. Is it January 1, 2015, or the first day of the first plan year beginning after January 1, 2015? If the applicable date is January 1, 2015, employers that maintain non-calendar year plans will need to start counting hours sooner rather than later. Employers that maintain non-calendar year plans may reasonably choose to wait for clarification before they start counting.

EBSA Advisory Opinion: Guidance on Revenue Sharing Arrangements

Many plans enter into revenue sharing arrangements with their service providers. Those service providers make available to plans a variety of investment options (e.g., mutual funds) and receive revenue sharing payments from these investments in the form of 12b-1 fees, shareholder and administrative services fees, or similar payments. In an advisory opinion issued in July (Adv. Op. 2013-03A), the Department of

Labor's Employee Benefit Security Administration (EBSA) examined a particular revenue sharing arrangement under which the service provider retains all of the payments but agrees to maintain a bookkeeping record of revenue sharing received in connection with the plan's investments. Those revenue sharing payments may be used to pay certain plan expenses, such as for the services of accountants, consultants, actuaries, or attorneys to the plan. The service provider deposits the revenue sharing payments into its general asset accounts and does not establish a special bank or custodial account to hold the revenue sharing payments. The service provider makes no representations to the plan fiduciaries or to any plan participants or beneficiaries that revenue sharing amounts it receives will be set aside for the benefit of the plan or that they represent a separate fund for payment of benefits or expenses under the plan.

The advisory opinion offers the following guidance on this and similar revenue sharing arrangements:

• While EBSA acknowledged it is possible that revenue sharing amounts received by a service provider can, in certain circumstances, be assets of the plan, EBSA concluded that revenue sharing payments recorded in the bookkeeping account in this instance are not plan assets before the plan actually receives them. The plan's contractual right to receive the amounts agreed to with the service provider or to have them applied to plan expenses, however, would be an asset of the plan.
• The advisory opinion points out that the responsible plan fiduciaries must evaluate whether a service provider's revenue sharing or other fee arrangements give rise to any non-exempted prohibited transactions under the Employee Retirement Income Security Act (ERISA). If a service provider, in its provision of services to a plan, is an ERISA fiduciary by virtue of providing investment advice for a fee and uses any of that authority, control, or responsibility to cause a plan to invest in funds that pay revenue sharing or other fees, it is possible that a non-exempted prohibited transaction would occur.
• Responsible plan fiduciaries must assure the compensation the plan pays directly or indirectly to a service provider is reasonable, taking into account the services provided to the plan as well as all fees or compensation received by the service provider in connection with the investment of plan assets, including any revenue sharing. Responsible plan fiduciaries must obtain sufficient information regarding all fees and other compensation the service provider receives with respect to the plan's investments to make an informed decision as to whether the service provider's compensation for services is no more than reasonable.
• Responsible plan fiduciaries must act prudently and in the best interests of plan participants and beneficiaries in the negotiation of the specific formula and methodology under which revenue sharing will be credited to the plan and paid back to the plan or to plan service providers. A plan fiduciary, prior to entering into such an arrangement, must understand the formula, methodology, and assumptions used by the service provider in arriving at the amounts to be returned to the plan or used to pay plan service providers. The plan fiduciaries must be capable of periodically monitoring the service provider to assure the amounts to which the plan may be entitled under the terms of the arrangement are correctly calculated and applied for the benefit of the plan.

PBGC Proposes Changes to Premium Due Dates

The Pension Benefit Guaranty Corporation (PBGC) proposed new regulations that would simplify the due date for premium payments. Under the proposed rule, the due date to pay annual premiums is October 15 for all types of plans. This would eliminate variations in due dates that exist under current regulations. In addition, the PBGC proposed regulations would provide for better coordination of the premium due date for terminating plans to avoid the situation where the premium's due date might be well after the plan termination and all termination distributions are complete.

CASES

Failure to Comply With Section 204(h) Notice Requirement in Cash Balance Conversion Does Not Result in Monetary Relief

Solvay Chemicals Inc. converted its traditional defined benefit plan into a cash balance plan. To comply with the requirements of ERISA Section 204(h), the company issued a six-page notice (204(h) Notice) to explain how the conversion to a cash balance plan worked and how any reductions in benefit accrual that would occur. Certain employees filed suit claiming the 204(h) Notice did not fully explain some of the changes and cutbacks made as a result of the conversion. The district court held the 204(h) Notice was deficient. Specifically, they found the 204(h) Notice did not adequately describe the changes in early retirement subsidies between the traditional plan and the cash balance formula. The issue in the current case is whether the violation of ERISA Section 204(h) results in a remedy for the employees. The employees requested that the early retirement subsidies be reinstated. ERISA Section 204(h) provides that a court may award benefits to which the employees would have been entitled only if the notice failure was "egregious." The term egregious is defined to mean either (i) the company's failure was within its control and was intentional or (ii) it was within the company's control and the company failed to promptly provide the required notice or information after discovery of an unintentional failure. The district court found the earliest time the company discovered its failure was when the employees filed the suit. Following the filing of the suit, the company sought additional advice from its ERISA counsel and actuaries and provided additional information. The district court therefore found the company's failure was not egregious. On appeal to the 10th Circuit Court of Appeals, the decision of the district court was upheld. The 10th Circuit rejected the employees' claim that the failure was intentional because the company testified it never intended to leave out details, outside lawyers and actuaries testified that the company's intent was to comply with the requirements of ERISA 204(h), and the outside lawyers and actuaries testified the company never pushed back against their advice and recommendations on what should be included in the 204(h) Notice. Thus the circuit court found the participants did not provide sufficient evidence to indicate that the failure was intentional. Further, the actions of the company to provide additional information to employees did not result in an unintentional error to become an egregious error.

While the company avoided any monetary recoveries to employees because of the 204(h) Notice failure, the case helps reinforce the position that a notice under ERISA Section 204(h) should be as complete as possible and describe every potential reduction in benefits so as to avoid what could be costly litigation. (*Jensen v. Solvay Chemicals Inc.*, 10th Cir., 2013)

Court Upholds Plan's Contractual Limitation Period

The U.S. Court of Appeals for the Sixth Circuit recently upheld a district court ruling that a long-term disability plan could bar a claim that exceeded its contractual limitation period. In this case, the plaintiff left employment with his employer in 2001 due to a variety of medical conditions. The plaintiff applied for and was denied long-term disability benefits because the claims administrator determined that nothing in the plaintiff's file suggested that he had been "continuously disabled." The plaintiff twice unsuccessfully appealed this benefit denial. In 2007, the plaintiff returned to work for his former employer, but after a year the plaintiff again left employment due to his medical conditions. Again he filed a claim for benefits under the long-term disability plan. This time his claim for benefits was successful. The claim administrator determined that his disability benefit would begin after he terminated employment in 2008. The plaintiff, however, sued the plan, arguing his disability benefit should have begun following his first termination of employment in 2001. The court upheld a district court ruling that the plan's contractual provision, requiring participants to file an ERISA claim within three years, barred the plaintiff's lawsuit. This case serves as a reminder that, to help protect the plan from liability, plan sponsors should include a contractual limitation period in their plan document. (*Engleson v. UNUM Life Insurance Co. of America*, 6th Cir., 2013)

Prenuptial Agreement Not an Effective Waiver of Spousal Rights

A recent decision by the U.S. Court of Appeals for the Eighth Circuit demonstrates the potential limitations of prenuptial agreements purporting to waive spousal rights to pension benefits, even when re-executed after a marriage has occurred and presented to a plan administrator. The couple in this case had been married and divorced from each other twice before they embarked on their third attempt at a successful marriage. Chastened, perhaps, by their previous marital failures, the couple executed a prenuptial agreement both before and after their third wedding. Under the agreement, the wife waived her rights to the husband's 401(k) plan account with his employer. The husband had previously designated his parents as beneficiaries of the account. Less than two years after their marriage, the couple had already begun the process of obtaining their third divorce when the husband died. Both the surviving wife and the parents filed a claim to the husband's 401(k) account, ultimately sending the dispute to the courts. The parents argued that their daughter-in-law had waived her spousal rights to the benefits when she signed the prenuptial agreement, giving them the right to the account as the designated beneficiaries. An Iowa district court disagreed, ruling that the prenuptial agreement was not an effective waiver of the wife's survivor rights because it did not satisfy the acknowledgment requirement of ERISA.

The appeals court agreed, finding the prenuptial agreement failed to inform the wife in clear and express terms that she both had a spousal right to receive the funds in her husband's 401(k) account and that she was waiving this right. Rather, the language in the agreement seemed to contemplate the future execution of a waiver. Because the prenuptial agreement failed to make it clear that, by executing the waiver in the document, the wife would not receive the funds to which she would otherwise be entitled, the court found that the prenuptial agreement failed to comply with the consent requirements of ERISA. As a result, the rights of the wife as surviving spouse prevailed over the designation of the parents as beneficiaries. (*MidAmerican Pension and Employee Benefits Plans Administrative Committee v. Cox*, 8th Cir. 2013)

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