EMPLOYMENT LAWSCENE ALERT: EMPLOYERS MUST IMMEDIATELY DECIDE WHETHER TO IMPLEMENT SEPTEMBER 1, 2020 PAYROLL TAX DEFERRAL

On August 8, 2020, President Trump issued an Executive Memorandum directing the Secretary of the Treasury to defer the withholding, deposit, and payment of the employee portion of the Social Security tax (6.2% of wages) for the period beginning on September 1 and ending on December 31, 2020. The deferral applies for employees whose pre-tax bi-weekly wages or compensation is less than $4,000. On an annualized basis, this equates to a salary not exceeding $104,000.

The IRS recently issued limited guidance on the implementation of the deferral. Open issues and takeaways are summarized below.

Additional Detail

In addition to calling for the deferral of the payroll tax, the Memorandum directs the Secretary to explore avenues for eliminating the taxpayers' obligation to repay the deferred taxes in the future. It should be noted that only Congress, not the Secretary, has the authority to waive taxes.

The Memorandum does not provide detail on how the payroll tax deferral will be implemented. In related interviews, the Secretary commented that, while he hoped that many companies would participate, he couldn't force employers to stop collecting and remitting payroll taxes. In other words, he suggested that the payroll tax deferral would be voluntary—a proposition not included in the Executive Memorandum.

Requests for Clarification

Uncertainty surrounding how to implement the payroll tax deferral resulted in requests from multiple trade groups for clarification, including an August 18 letter signed by 33 trade groups, including the U.S. Chamber of Commerce. The letter, submitted to the Secretary and to the respective leader of the U.S. Senate and of the U.S. House of Representatives, notes that under current law, the Memorandum creates a substantial tax liability for employees at the end of the deferral period.

While the stated purpose of the Memorandum was to provide wage earners with additional available spending money, unless Congress later acts to forgive liability for the deferred payroll tax, the affected earners will owe an increased tax bill next year. As the U.S. Chamber of Commerce letter maintains, the deferral "threatens to impose hardship on employees who will face a tax bill" in an amount of double the usual payroll deduction for Social Security (amounting to 12.4% of employee wages) in the first four months of 2021.

The following chart illustrates the U.S. Chamber of Commerce's assessment of the magnitude of the potential tax bill for employees compared to the immediate benefit of the deferral:

Annual Income	**Bi-Weekly Pay**	**Increase in Take-Home Pay by Pay Period**	**Tax Bill Due in 2021 (based on 9 pay periods)**
$35,000	$1,346.15	$83.46	$751.15
$50,000	$1,923.08	$119.23	$1,073.08
$75,000	$2,884.62	$178.85	$1,609.62
$104,000	$4,000	$248.00	$2,232.00

The U.S. Chamber of Commerce letter further states that many of its employer members would likely decline to implement the deferral, choosing instead to continue to withhold and remit to the government the payroll taxes required by law.

IRS Notice 2020-65

Late in the afternoon on August 28, 2020, the IRS issued Notice 2020-65 to provide guidance regarding the payroll tax deferral. The Notice clarifies that any deferred amounts must be recouped by being collected from employee wages and repaid during the period between January 1, 2021 and April 30, 2021. Interest and penalties begin to accrue May 1, 2021 on any unpaid amounts. While the Notice is silent on the issue, it is presumed, because of the normal operation of payroll tax law, that employers would be responsible for paying any interest and penalties that accrue, in addition to paying any underlying deferred amounts that cannot be collected from employees.

Some questions about how to implement the deferral remain unanswered by the IRS guidance. Specifically, the guidance addresses neither self-employed individuals nor the method for reporting the deferral of taxes on IRS Forms 941 or W2. The guidance is also silent on how to collect deferred tax for an individual who is no longer employed for all or part of the 2021 repayment period. Staffing agencies, in particular, are concerned about employer exposure to the repayment cost in the event that employees for whom taxes were deferred are no longer employed during the repayment period. It is not clear that deducting the amount owed from an employee's final paycheck would be specifically permitted under either federal or state law, or any applicable bargaining agreements.

Decisions, Decisions

While some employers may welcome the ability to offer the payroll tax deferral to employees as a current relief measure, others may view with some reluctance the prospect of exposure to additional payroll tax costs coupled with the need to re-code payroll software effective September 1, 2020, January 1, 2021, and May 1, 2021. Implementing the current deferral and future double collection would also require careful and accurate communication to employees.

The IRS guidance leaves the door open for employers to avoid, rather than to implement the deferral, and to proceed, instead, to process payroll according the normal procedures. In the language of the guidance, an employer may, "if necessary, . . . make arrangements to otherwise collect the total Applicable Taxes from the employee."

O'Neil, Cannon, Hollman, DeJong and Laing remains open and ready to assist you. To discuss how the Memorandum, IRS guidance, and practical considerations relevant to the payroll tax deferral may apply to your business objectives and circumstances, please speak to your regular OCHDL contact.

EMPLOYMENT LAWSCENE ALERT: ACTION REQUIRED BY AUGUST 31, 2020 FOR CERTAIN RETIREMENT-RELATED CARES ACT RELIEF

An August 31, 2020 deadline applies both to individual retirement account participants who want to repay a required minimum distribution received in 2020 and to employer plan sponsors who wish to reduce or suspend certain 401(k) or 403(b) safe harbor employer contributions. Details on each of these special tax relief provisions are summarized below.

Employers and individuals who wish to avail themselves of these special tax relief provisions should take prompt action.

Deadline for Repayment of Certain Waived 2020 Required Minimum Distributions

As we've described previously, tax law generally requires a 401(k), 403(b), or 457(b) retirement plan participant, or IRA owner, to take required minimum distributions (RMDs) annually once the owner reaches age 72 (or 70 ½ under the SECURE Act).

In late March 2020, the CARES Act waived the requirement to take an RMD from a retirement plan or IRA in 2020. For retirement account owners who had already taken 2020 RMDs and did not need them, the CARES Act provided a way to return them. Although RMDs are not usually eligible for rollover treatment, the CARES Act repayment mechanism is to treat the waived RMDs as if they are distributions eligible for rollover. Instead of actually rolling the amount over to a different plan, however, the CARES Act permits a 2020 waived RMD amount to be repaid only to the same account that paid it out. Any repayment, as described in the CARES Act, was required to take place within the standard 60-day window for making a rollover from one tax-favored account into another.

Because the CARES Act was passed in late March, the 60-day repayment period had by then already expired for those who had taken an RMD in early January 2020. The more recent IRS Notice 2020-51 extends the 60-day window period, so that any waived RMDs received on or after January 1, 2020 may now be repaid, provided that such repayment occurs by August 31, 2020.

Employer plan sponsors may also wish to review whether their plan document should be amended by the deadline to accept RMD repayments if their participant population desires to repay previously-distributed 2020 RMDs to the plan.

Employer Deadline to Reduce or Suspend 401(k) or 403(b) Safe Harbor Contributions

In a separate announcement, Notice 2020-52, the IRS has provided special relief to employer plan sponsors of 401(k) and 403(b) retirement plans who wish to make a mid-year reduction or suspension of safe harbor nonelective employer contributions. The ability to take such action expires on August 31, 2020 and should be properly documented as of that date.

Background

More and more employer sponsors of workplace retirement plans, in recent years, have chosen to adopt a “safe harbor” employer contribution feature. The key advantage of safe harbor status for a tax-qualified retirement plan is that the plan is deemed to treat highly and non-highly compensated employees fairly, with respect to one another. It is therefore exempt from the otherwise applicable annual nondiscrimination testing.

In exchange for safe harbor status and the perk of avoiding complex and sometimes costly nondiscrimination testing, a safe harbor plan must meet certain requirements, including committing to provide a minimum employer contribution or formula, immediate vesting of the contributions, and the provision of an informational notice regarding the contributions before the beginning of the plan year (a safe harbor notice).

The Safe Harbor 12-Month Rule

Typically, once a safe harbor provision is adopted for a retirement plan, it must be in effect for all 12 months of the plan year. This requirement is intended to prevent employers from avoiding nondiscrimination testing if they do not honor the corresponding requirement to contribute to the plan for the benefit of participants.

Generally, there are two exceptions to the 12-month rule that permit a mid-year suspension or reduction of the safe harbor contribution:

1. The first applies if the employer is operating at an economic loss for the plan year.
2. The second applies if the safe harbor notice explicitly reserves to the employer the right to amend, reduce, or suspend the safe harbor contribution during the year.

Under either exception, an additional notice of amendment, reduction, or suspension must be provided to all participants at least 30 days in advance of the effective date of such action. As a result of any mid-year change to a safe harbor contribution, a plan is required to pass nondiscrimination testing in lieu of relying on the safe harbor testing exemption for the year.

Temporary Relief Related to Mid-Year Safe Harbor Nonelective Contribution Changes and Notices

IRS Notice 2020-52 provides special relief under which employers may make a prospective mid-year suspension or reduction of safe harbor nonelective contributions to 401(k) and 403(b) plans after March 13, 2020, for the balance of the year, regardless of whether the employer has satisfied either the requirement of incurring an economic loss or of previously providing a safe harbor notice reserving the right to change contributions.

Additionally, for safe harbor nonelective contribution plans, rather than providing the revised safe harbor notice at least 30 days before the effective date of the suspension or reduction, the notice must be provided by August 31, 2020.

This relief is time-limited, however. To take advantage of these special rules, a plan amendment suspending or reducing the safe harbor contribution must be adopted by August 31, 2020.

Note that the relief provided in IRS Notice 2020-52 does not apply to a mid-year reduction of 401(k) safe harbor *matching* contributions. This is because of the IRS’s view that matching contribution levels as communicated to employees directly affect employee decisions regarding elective contributions and should therefore not be changed.

Note also that this article does not address the implications of certain SECURE Act changes to the safe harbor notice requirement, of the impact of IRS Notice 2020-52 thereon.

Conclusion

The temporary relief provided in IRS Notices 2020-51 and 2020-52 will respectively assist individual taxpayers seeking to avoid taking RMDs in 2020, and employer plan sponsors seeking 2020 cost reductions. In either case, action to take advantage of the relief must be taken by August 31, 2020.

The attorneys of the Labor and Employment Group of O'Neil Cannon are actively monitoring COVID-19 developments and are available to assist employers with related employment law and employee benefit plan compliance matters. Please contact us if you need assistance in amending your employer-sponsored retirement plan to accommodate mid-year safe harbor changes or the return of 2020 RMDs.

EMPLOYMENT LAWSCENE ALERT: IRS SAYS REDUCED-COST OR FREE COVID-19 TESTING OR TREATMENT WON'T PREVENT INDIVIDUALS FROM MAKING OR RECEIVING HSA CONTRIBUTIONS

In recent guidance, the IRS noted the "unprecedented public health emergency posed by COVID-19" (the disease that results from the 2019 Novel Coronavirus), and the need to remove potential administrative and financial barriers to COVID-19 testing and treatment under the health savings account (HSA) rules.

Issued on March 11, 2020, IRS Notice 2020-15 responds to employer uncertainty as to whether a health plan providing for reduced-cost COVID-19 testing—for individuals who have not yet met their annual deductibles—remains an HSA-compatible high-deductible health plan (HDHP).

That uncertainty arose from the recent wave of insurer and state announcements of the waiver of out-of-pocket costs for COVID-19 testing (and, in some cases, for treatment). Cost-sharing waivers apply, as of this writing, in at least 32 states, including for most, but not all, insurers in Wisconsin. Insurers have agreed to waive cost sharing due, variously, to voluntary agreements by major insurers, state mandates, or state-insurer agreements.

No-cost COVID-19 testing will be required by all private health plans now that President Trump has signed the Families First Coronavirus Response Act.

HSA-Compatible Coverage, Generally

As we described in a prior post, an HSA is a tax-favored account established to receive contributions from an employee, an employer, or both.

To be eligible to make (or receive) HSA contributions, an individual must be covered only under the HDHP and my not have any other coverage (including reduced-cost services), unless such other coverage is expressly permitted by the IRS.

Certain "preventive care" services are specifically permitted and are not considered to constitute "other" health coverage that would disqualify an individual from HSA eligibility. In July of 2019, the IRS expanded the list of "preventive care" to include fourteen additional items and services intended to prevent the worsening of certain chronic medical conditions.

HSA-Compatible Coverage Now Includes Coronavirus-related Services

The result of the newly-issued IRS Notice 2020-15 is that an individual who is covered by an HDHP will not lose eligibility to make (or receive) tax-favored HSA contributions merely because the HDHP permits pre-deductible COVID-19 testing and treatment with reduced (or no) employee cost-sharing. HSA-eligible individuals may continue to contribute to an HSA regardless of whether the HDHP offers, or the individual receives, a reduced-cost or no-cost COVID-19 test or treatment.

Be Aware That:

- As in the past, any vaccination costs continue to count as preventive care and can paid for by the plan at any time during the year, without regard to whether the deductible has been met.
- As recently confirmed by the Centers for Medicare and Medicaid, the costs of certain COVID-19 treatments and services, including testing, isolation, quarantine, and vaccination, are generally covered as essential healthcare benefits under Affordable Care Act rules for individual and small group health plans.
- Self-funded group health plans are not required to waive COVID-19 cost-sharing under the state mandates or insurer agreements (but are impacted under the federal Families First Coronavirus Response Act).

The text of the IRS Notice is available here.

The attorneys of the Labor and Employment Group of O'Neil, Cannon, Hollman, DeJong and Laing are actively monitoring COVID-19 developments and are available to assist employers with related employment law and employee benefit plan compliance matters.

EMPLOYMENT LAWSCENE ALERT: REVIEW YOUR COMPANY’S “TOP-HAT FILING” STATUS NOW TO AVOID INCREASED FORM 5500 PENALTIES

Companies that have entered into arrangements (1) to pay deferred compensation to key employees (including owners), or (2) to provide employee benefits specifically for apprentices or trainees should immediately determine whether a “top-hat filing” is required, and, if so, whether it has been properly filed with the Department of Labor. Two very recent legal developments—increased penalties and a new filing search tool—indicate that enforcement activity on top-hat filing compliance is increasing. Penalties for not filing can be extremely costly, and the penalties have been increased, effective January 15, 2020. Fortunately, a low-cost correction option is available for corrections made prior to a DOL assessment of penalties.

Top-Hat Overview

A top-hat filing is a short informational submission to the DOL that describes the company’s contact information and the nature of the sponsored plan. It is legally required to be submitted with respect to any compensation arrangement for key management and owner employees (or employee benefit plans provided only to apprentices or trainees) that constitutes a top-hat plan. So named in apparent reference to gentility as evoked by Lincoln-era fashion standards, a top-hat plan is an agreement or plan maintained by an employer primarily for the purpose of providing deferred compensation to a select group of key employees, apprentices, or trainees.

The term “select group of management or highly compensated employees” is not clearly defined, but must, instead, be determined in the context of the particular facts and circumstances that apply to the employer. Neither the IRS definition of “highly-compensated employee” or of “key employee” applies in determining whether a compensation arrangement is a top-hat plan. Instead, relevant factors include the duties and responsibilities of the employee and the level of the employee’s compensation as compared to the compensation of the employer’s work force, in general.

Top-Hat Filing – Required within 120 Days of Plan Effective Date

In general, all employer-provided benefits are subject to ERISA’s requirements, unless an exception applies. In the case of top-hat payment arrangements, DOL guidance has expressed that “certain individuals, by virtue of their position or compensation level, have the ability to affect or substantially influence, through negotiation or otherwise, the design and operation of their deferred compensation plan, taking into consideration any risks attendant thereto, and therefore would not need [all of] the substantive rights and protections of" ERISA. The DOL also permits this lower-protection status for arrangements that provide employee benefits (including health benefits) only to apprentices or trainees, or both.

In light of the reduced need for ERISA protections for these plans, the DOL authorizes an exemption from the otherwise-applicable ERISA mandates regarding participation, vesting, funding, and fiduciary rules. Importantly, an additional exemption from ERISA's reporting and disclosure rules is also available, but *only if* a "top-hat filing" is submitted to the DOL within 120 days of the initial effective date of such plan.

Because ERISA's reporting and disclosure rules include the requirement to file an annual Form 5500 to the DOL, this annual Form 5500 filing requirement continues to apply to a top-hat plan unless a top-hat filing has been timely submitted. Alternately, an initial failure to submit a top-hat filing can generally be corrected, retroactively, for a relatively small compliance fee.

Form 5500 Penalties at an All-Time High

An employer that fails to timely file a Form 5500 may be subject to a DOL penalty of $2,233 per day (as adjusted annually for inflation). This new penalty amount of $2,233 per day is effective January 15, 2020. (For the prior year, the penalty amount had been $2,194 per day). This is not a typographical error. The law applies these penalty amounts *per day* for each day past the required filing date(s). The penalties are cumulative and become exponentially large for failures stretching over multiple years. While an aggregate penalty assessment could likely be negotiated downward by experienced ERISA legal counsel, an assessed DOL penalty for a late Form 5500 is guaranteed to be large.

The IRS imposes separate penalties for the failure to timely file a Form 5500, unless a showing of reasonable cause is made. Until recently, the IRS penalty was $25 for each day of the failure up to a maximum penalty of $15,000 per year. Under the Setting Every Community Up for Retirement Enhancement (SECURE Act) enacted on December 20, 2019, however, the IRS penalties for a late Form 5500 have increased tenfold to $250 per day, up to an annual maximum of $150,000. These increased IRS penalties apply for any Form 5500 due to be filed on and after January 1, 2020.

New DOL Top-Hat Filing Search Tool

Earlier this week, the DOL published a new online search tool to enable the public to search for top-hat filings. The search tool is available here. Results can be printed or downloaded to Excel.

Prior to the DOL making the search tool available, generally only benefits professionals and practitioners ever searched for top-hat filings, and then only via a website maintained by a private company that regularly obtained the information from the DOL through Freedom of Information Act Requests.

The issuance of the public DOL search tool is a positive development that will assist employers in confirming their top-hat filing compliance status. Of course, this increased access likely also signals increased DOL interest in enforcing late Form 5500 penalties for those employers that have not timely filed a top-hat statement. In light of the ease of searching, it will now be harder for employers to reasonably contend that they were unaware that a top-hat filing had not been submitted. Similarly, it is conceivable that plaintiffs' attorneys or disgruntled employees could use the tool themselves to determine whether a company is likely out of compliance with the top-hat filing, and therefore, the Form 5500 filing, rules. If this knowledge were used to inform the DOL, which, in turn, could trigger a penalty assessment, the penalty amounts could be devastating.

Correction Option

If you determine or suspect that your company has inadvertently failed to submit a top-hat filing for a covered top-hat plan, take steps right away to amend this oversight by submitting a delinquent filer voluntary compliance application. If you catch the error before the DOL has assessed a penalty, then you can retroactively correct the issue for a fee of only $750 for a single year (or a maximum of $1,500 for multiple years). The IRS generally accepts this same correction method as sufficient to avoid the separate IRS Form 5500 penalties, as well. Indeed, this DOL correction method often works to abate the IRS penalties after these have already been assessed.

Conclusion

It is common for companies that implement deferred compensation arrangements to consider the tax implications of such arrangement, including, for example, the application of Internal Revenue Code Section 409A. Equally important, however, is consideration of the other federal law that may govern such arrangements—ERISA. It is simply not true that all compensation agreements for key employees are exempt from ERISA's requirements. Failure to anticipate this reality—and to submit a top-hat filing when required—exposes the employer to significant Form 5500 penalties.

To avoid these penalties, check on your company's top-hat filing compliance now. The attorneys of the OCDHL Employment Law Team can assist you with assessing whether your company's key employee compensation agreements constitute top-hat plans within the meaning of ERISA, or whether an exemption may apply. If you maintain a top-hat plan for which no top-hat filing was ever submitted, we can assist in correcting the inadvertently missed prior filings, thereby potentially eliminating the existing exposure to thousands of dollars.

EMPLOYMENT LAWSCENE ALERT: EIGHTH CIRCUIT HOLDS THAT AN SPD CAN FUNCTION AS A PLAN DOCUMENT

A federal appellate court has ruled, in *MBI Energy Services v. Hoch*, decided in July 2019, that a single document may serve as both the summary plan description (SPD) and the formal plan document for an ERISA welfare benefit plan.

In this case, the plan sponsor of a self-insured group health plan paid benefits on behalf of a participant for medical injuries sustained in an accident. Subsequently, the participant settled a tort claim with a third party who allegedly caused the accident. The settlement amount exceeded the amount of the plan-paid medical expenses and the plan sponsor sought reimbursement.

ERISA Requires a Plan Document

Under ERISA, the requirement that “every employee benefit shall be established and maintained pursuant to a written instrument” is understood to mean that the terms of each benefit program must be memorialized in a written plan document. ERISA further requires the plan sponsor to provide to each plan participant an SPD that briefly and clearly summarizes the terms of the plan document.

In some cases, plan sponsors do not offer two separate documents (a plan document and an SPD), but rely, instead, on a single combined document that purports to function both as the plan document and as the SPD.

Several courts have argued that a combined Plan document and SPD is unacceptable on the grounds that it is not possible for a document to summarize itself. Nonetheless, in the self-insured medical plan context (where coverage exclusions and limitations are difficult to summarize), it is common to have a single document that serves as both the plan document and the SPD.

Where’s the Plan?

While the employer in the *MBI Energy Services* case could point to no document clearly identified as the “plan,” there was an administrative services agreement (ASA) between the employer and the plan’s claims administrator indicating that the plan benefits, terms, and conditions were set forth in an attached exhibited – the SPD. Along with the benefit provisions and ERISA-mandated language, the SPD contained sections addressing the rights of subrogation, reimbursement, and assignment. The SPD stated, in part, that if a participant “makes any recovery from a third party . . . whether by judgment, settlement or otherwise,” the participant must reimburse the plan sponsor “to the full extent of any benefits paid” by the plan.

The Arguments

The participant argued that the SPD was not a valid plan document and that the employer therefore had no right to reimbursement. Instead, the participant asserted that the SPD was only a summary of, and in conflict with the terms of, the ASA, which the participant contended was the controlling plan document. The participant’s argument was rooted in the Supreme Court’s reasoning, in its 2011 *CIGNA v. Amara* ruling, that “’summary documents, important as they are, provide communication with beneficiaries *about* the plan, but that their statements do not themselves constitute the *terms* of the plan.”

The plan sponsor, on the other hand, argued that the SPD functioned as both the SPD and the plan document and that the SPD’s reimbursement language gave the plan an equitable lien on the participant’s recovery proceeds.

The Ruling

The Eighth Circuit disagreed with the participant’s contention that the SPD was unenforceable because it conflicted with the ASA, pointing out that the ASA was silent as to reimbursement and expressly incorporated the terms and conditions of the SPD. The court thereby joined other circuits in distinguishing *CIGNA v. Amara* (a retirement plan matter in which both a plan document *and* an SPD were present) and concluding that, absent a formal plan document, the SPD may function as the plan document.

Specifically, the court rejected as “nonsensical” any interpretation that renders no plan document at all under the terms of ERISA and concluded that the label of SPD is not dispositive. Where no other source of benefits exists, the SPD *is* the formal plan document.

The court also pointed out that it would be inequitable to allow the participant to receive benefits according to the SPD but not hold him to the reimbursement responsibilities set forth in that same document. It concluded that, since the SPD was the plan’s written instrument, the participant was bound by its terms and obligated to reimburse the plan.

As a result, the participant was required to reimburse the self-funded employee benefit plan for $45,474 in medical benefits the plan had paid.

Implications

Since the U.S. Supreme Court's *CIGNA v. Amara* ruling, plan sponsors of self-insured plans have wondered whether the common practice of using a single document as both the plan and the SPD may permissibly continue. The Eighth Circuit's *MBI Energy Services* ruling adds to a growing list of cases finding that an SPD can function as an enforceable ERISA welfare plan document in the absence of a separate additional document.

Plan sponsors should take note that identifying the controlling language relevant to a given employee benefit plan is not always clear cut. In some cases (as here), the plans terms may be contained within a single document. In other instances, the terms of an ERISA plan may be inferred from a series of documents, none of which is clearly labeled as a plan.

Do your Plan's Documents Protect You?

All plan sponsors are advised to review whether their documents for ERISA welfare plans (such as group health, dental, vision, disability, and life plans) not only comply with ERISA, but also whether they reflect the employer-specific disclosure requirements and employer-protective statements, which are typically *not* included in documents prepared by insurers or third-party administrators.

In many cases, it is advisable to streamline multiple separate ERISA benefits into a single so-called Wrap Plan document, which 'wraps around' and supplements the other documents to become the SPD. A Wrap Plan can help employers to minimize the risk of financial penalties and lawsuits and streamlines certain reporting and amendment requirements.

The attorneys of the Employment Law Group of O'Neil, Cannon, Hollman, DeJong and Laing can assist in reviewing and providing counsel relating to the documentation and operation of all employer-sponsored employee benefit and compensation plans.

EMPLOYMENT LAWSCENE ALERT: IRS EXPANDS LIST OF HSA-COMPATIBLE PREVENTIVE CARE SERVICES

The IRS recently issued guidance expanding the types of preventive care services that can be provided by a high-deductible health plan (HDHP), before the deductible is met, without eliminating a covered individual's eligibility to participate in a Health Savings Account (HSA). The new guidance was published on July 17, 2019 and took legal effect on that same day.

Employers who sponsor HDHPs should now consider whether any plan documentation or communication changes are required to implement the expanded preventive care coverage rules. Alternately, employers who have not previously adopted a HDHP should assess whether the new rules may now make the HDHP/HSA model a more attractive way to control health care costs.

Background
An HSA is a tax-favored account that may receive contributions from an employee, an employer, or both. HSAs are subject to various rules that govern the individual account holder's eligibility to make and receive contributions and whether or not withdrawals are taxable.

To be eligible for HSA contributions, an individual must be covered under a HDHP and may generally not have any health coverage other than HDHP coverage. Certain preventive care services, however, are not considered to constitute health coverage so as to disqualify an individual from HSA eligibility.

Previously, preventive care (within the meaning of the HSA and HDHP rules) has not included any service or benefit intended to treat an *existing* illness, injury, or condition.

The IRS is aware, however, that cost barriers for care have resulted in the failure by some individuals who are diagnosed with certain chronic health conditions to seek or to use effective and necessary care that would prevent exacerbation of such conditions. Accordingly, and in consultation with the U.S. Department of Health and Human Services (HHS), the IRS determined that certain medical care services received and items purchased, including prescription drugs, should now be classified as preventive care for someone with the corresponding chronic condition.

Newly Established HSA-Compatible Preventive Care
To address the stated concerns, the expanded list of HSA-Compatible preventive care expenses includes fourteen cost-effective items and services that are likely to prevent the worsening of eleven specified chronic conditions, as follows:

Preventive Care for Specified Conditions	**For Individuals Diagnosed with**
Angiotensin Converting Enzyme (ACE) inhibitors	Congestive heart failure, diabetes, or coronary artery disease
Anti-resorptive therapy	Osteoporosis or osteopenia
Blood pressure monitor	Congestive heart failure or coronary artery disease
Inhaled corticosteroids	Asthma
Insulin and other glucose-lowering agents	Diabetes

Retinopathy screening	Diabetes
Peak flow meter	Asthma
Glucometer	Diabetes
Hemoglobin A1c testing	Diabetes
International Normalized Ratio (INR) testing	Liver disease or bleeding disorders
Low-density Lipoprotein (LDL) testing	Heart disease
Selective Serotonin Reuptake Inhibitors (SSRIs)	Depression
Statins	Heart disease and diabetes

The IRS and HHS will together review the list approximately every five to ten years to determine whether any items or services should be removed or added.

Changes Arose from Executive Order and Policy Advocacy

The immediate impetus of the change is Section 6 of Executive Order 13877, "Improving Price and Quality Transparently in American Healthcare to Put Patients First," which was signed by President Trump on June 24, 2019, and which mandated the issuance of guidance permitting HSAs to cover low-cost preventive care to help "maintain health status for individuals with chronic conditions."

The change also reflects the efforts of various health-policy advisors and advocates, who have long called for allowing first-dollar HDHP coverage for targeted, evidence-based, preventive services that prevent chronic disease progression and related complications.

Key HDHP Sponsor Issues and Next Steps

- In preparation for the 2020 open enrollment season, employer-sponsors of HDHPs should work to educate employees and dependents to assist them in understanding and benefitting from the new pre-deductible preventive care services.
- Sponsors of HDHPs should review whether or not existing plan documentation should be amended to encompass the expanded categories of covered care (or whether the current definitions remain legally sufficient).
- Because the out-of-pocket costs for some types of chronic care will now shift to the employer, sponsors of HDHPs should analyze whether the current deductible and premium levels are sufficient to meet the increased benefit expenses, or whether adjustments are warranted.
- Employers who offer both HDHPs/HSAs and on-site health clinics may provide only preventive care services in the on-site clinic in order to avoid jeopardizing employee HSA eligibility. Affected employers may now reconsider and expand the types of pre-deductible services to be provided to employees in the on-site clinic.
- Increased coverage of chronic condition expenses may increase the attractiveness of HDHP coverage to participants who are managing chronic conditions. The new rules

may provide an opportunity to either increase future employee participation in, or to newly adopt, HDHP/HSA coverage.

EMPLOYMENT LAWSCENE ALERT: NEW RULE WILL PERMIT EMPLOYER REIMBURSEMENT OF EMPLOYEES’ INDIVIDUAL ACA COVERAGE PREMIUMS

Beginning January 1, 2020, employers will have the option to reimburse employees’ individual ACA Exchange (or Marketplace) health insurance premiums under an employer-sponsored Health Reimbursement Arrangement (HRA).

This is a significant change from current rules, which generally permit an HRA to reimburse only group (not individual) health insurance coverage, and which prohibit employer reimbursement of any health insurance coverage provided through the ACA Exchange.

<u>HRA Overview</u>
An HRA is a type of account-based plan that an employer may use to provide pre-tax reimbursement, up to employer-determined annual limits, of certain employee medical care expenses. Under applicable law, an HRA is a self-funded health care plan, which may be funded only by employer (not employee) dollars. An HRA is subject to ERISA, HIPAA, and certain IRS rules, including the nondiscrimination requirements that prohibit discrimination in favor of highly compensated employees.

<u>What’s Old is New Again</u>
Under final regulations issued jointly, last week, by the United States Departments of Treasury, Labor, and Health and Human Services (the Departments), Employers can once again reimburse certain individual employee health insurance expenses on a pre-tax basis. This practice was broadly permitted under IRS rules in effect from 1961 through January of 2014, when the IRS put a sudden halt to the practice on the grounds that it violated the Affordable Care Act.

<u>With Some Twists</u>
Prior to 2014, employers could directly reimburse an employee for the cost of that employee’s individual insurance coverage premiums. No additional benefit plan or plan document was required. Under the new rules, employer reimbursements of individual insurance premiums may not be made directly, but must instead flow through a documented HRA program. The HRA must conform in form and operation with applicable Department

rules.
Under the law in effect over the last few years, an HRA could reimburse group health plan insurance premiums only if it were “integrated with” an ACA-compliant employer-sponsored group health plan. Under the rules that will take effect January 1, 2020, HRA “integration” with ACA-compliant individual coverage will be available for the first time.

Why are the HRA Rules Changing?
The final regulations issued jointly by the three Departments last week ultimately result from an October 2017 Presidential Executive Order intended to expand “healthcare choice” and flexibility. HRAs were one of three priorities identified in President Trump’s Executive Order 13813, which directed the Departments to consider proposing regulations or revising guidance as needed “to expand employers’ ability to offer HRAs to their employees, and to allow HRAs to be used in conjunction with non-group coverage.”

Key Requirements
The final regulations exceed 200 pages and provide extensive detail on the requirements applicable to the new individual coverage HRAs (ICHRAs). Among these are the following six key conditions, which must be satisfied in order to successfully integrate an HRA with individual health insurance coverage:

- All individuals covered by an ICHRA must be enrolled in individual coverage through the Exchange.
- The employer may not offer an ICHRA to the same class of employees to whom it offers group health plan coverage. This means that an employee in a particular classification may not be given a choice between a traditional group health plan and an ICHRA. Under a related rule, employers are prohibited from steering participants with adverse health factors into individual, rather than into group, coverage.
- An ICHRA must be offered in both the same amount and under the same terms and conditions to all employees. The HRA may not be more generous or less generous to some individuals based on an adverse health factor.
- The ICHRA must offer an opt-out provision so that an employee may choose to waive ICHRA HRA coverage. This condition is intended to preserve an individual’s eligibility for a premium tax credit for coverage obtained on the Exchange under certain circumstances, such as when the ICHRA offered is either unaffordable or does not provide minimum value in accordance with ACA standards.
- Claims for reimbursement under an ICHRA must be substantiated and confirmed to relate to the cost of individual Exchange health insurance premiums. An employer may rely on an employee’s attestation to this effect, and model attestation forms have been provided by the Departments. If an ICHRA sponsor learns of an incorrect or false attestation, future reimbursements relating to the relevant period may be denied.
- Participants potentially eligible to participate in an ICHRA must be provided with a written notice at least 90 days before the beginning of each plan year (with some exceptions for a shorter notice period in for an initial year of eligibility). The final regulations specify the content that must be provided in the notice.

Limited Time to Prepare

In order for employers to reimburse employees' purchase of individual ACA-regulated health insurance by January 1, 2020, there is much work to do in relatively little time. Before the November 1 start date of the open enrollment period for 2020 ACA coverage:

- Employers must adopt (or amend existing) HRA Plan documents to comply with the new requirements;
- Employers, as well as Exchanges will need to work to communicate the changes to eligible individuals; and
- All separate State-facilitated Exchanges, as well as the Federal Exchanges must implement any required website coding and enrollment procedures.

The State-facilitated Exchanges have been concerned about a possible 2020 rollout since that date was initially mentioned in proposed rules issued late last year. This April, the administrators of all 12 State Exchanges asked the Departments to postpone the effective date. In response, the Departments have promised to provide technical assistance to the Exchanges to facilitate timely implementation of the new rules. Nonetheless, the final regulations are extremely detailed and complex. Whether, and to what extent, employers (and Exchanges) are able to embrace ICHRA reimbursement of individual health insurance premiums remains to be seen.

The attorneys of the Employment Law team of O'Neil, Cannon, Hollman, DeJong and Laing are closely following these new developments and are prepared to discuss how the change in HRA rules may impact your strategy regarding employee benefits offerings, ACA compliance, or how to amend an existing HRA or MERP (medical expense reimbursement plan) or to adopt a new HRA document to prepare for the reimbursement of individual coverage.

EMPLOYMENT LAWSCENE ALERT: IRS ISSUES A SECOND SET OF APRIL 2019 CHANGES TO RETIREMENT PLAN CORRECTION PROGRAM

The IRS Employee Plans division on Friday, April 19, released an updated version of its comprehensive retirement plan correction protocol. Although touted as a "limited update" to the Employee Plan Compliance Resolution System, or EPCRS, the changes contained in this new Revenue Procedure 2019-19 nonetheless offer substantial savings opportunities for certain employer sponsors of 401(k), 403(b), and profit-sharing plans, and employee stock ownership plans (ESOPs).

The update is effective immediately, and is notable for being the second change in the EPCRS rules to take effect in April 2019. Under a previously-issued update to the program, a new online-only submission requirement took effect on April 1, 2019. As of that date, plan sponsors are no longer permitted to submit EPCRS correction applications or payments by mail.

Bottom Line

The effect of the April 19 update is to expand the circumstances under which a plan sponsor is permitted to correct a self-identified error under the self-correction program (SCP), rather than having to submit a formal application, and accompanying fee, to the IRS.

This expansion of the opportunities for self-correction is a welcome opportunity for plan sponsors who become aware of certain plan compliance failures involving the language of the plan document as well as particular types of errors in the operation of participant loan programs. Correction of the specified errors may now be made on a less formal basis. Provided that the proper correction protocol is followed and documented, a correction can now be completed without having to pay the usual IRS submission fee, which ranges from $1,500 to $3,500.

EPCRS Background

The purpose of the IRS EPCRS program, generally, is to provide a system of correction programs and procedures for sponsors of tax-qualified retirement plans that have fallen outside of the qualification requirements either because of errors in the language of the plan document or because of mistakes in how the plan is operated. The EPCRS correction program permits plan sponsors to correct these errors and thereby to continue to offer retirement benefits to their employees on a tax-favored basis.

Depending on the nature and severity of a retirement plan compliance error, three different EPCRS programs exist, each with slightly different rules:

- SCP. For the least significant errors, the Self Correction Program (SCP) permits a plan sponsor to self-correct the error without paying any fee or sanction and without submitting any documentation to the IRS. Even though no documents are submitted to the IRS under the SCP program, it is important that the proper self-correction protocols described by the IRS are followed. An improper or undocumented self-correction provides no future IRS audit protection. A proper retirement plan self-correction, however, will protect a plan sponsor from future fees or penalties related to the properly-corrected error.

- VCP. For more significant compliance failures, or for failures not corrected within a specified time period, the only way to receive approval of a correction is to participate in the Voluntary Compliance Program (VCP). This program requires that a description of the error, and of its correction, be submitted to the IRS for formal approval. To use this program, a plan sponsor must pay a fee to the IRS. Under the recently-amended fee structure, the amount of the fee depends solely on the amount of plan assets and ranges from $1,500 (for plans with less than $500,000 in assets) to $3,500 (for plans with more than $10,000,000 in assets).

- Audit CAP. If it is the IRS, rather than the plan sponsor, who identifies a compliance error, then the only permitted correction program is the more expensive Audit CAP program. Errors can be corrected under Audit CAP if the IRS identifies an error during an audit. Under Audit CAP, the penalties imposed in order to retain the retirement plan's tax-qualification will be larger than under the VCP program, and will vary, based upon the nature and extent of the compliance error, the severity of the error.

Potential Opportunity to Make Key Corrections at a Lower Cost

The Treasury Department and IRS expect to continue to update the EPCRS program, in whole or in part, from time to time. Given the ever-changing and highly fact-specific nature of the IRS correction program, the severely adverse threat of plan tax-disqualification, and the need to determine the most effective correction strategy, plan sponsors who suspect or know that a retirement plan has a compliance error are advised to work confidentially with legal counsel specifically experienced in this area of practice. Because an error cannot be corrected under either the SCP or VCP programs after an IRS audit has begun, it is always best to respond to a compliance error quickly and proactively.

Now that the opportunities for self-correction have been expanded, there is no time like the present for plan sponsors to review their tax-qualified plan documentation and operations. Because more types of compliance errors can now be self-corrected, the cost of bringing an employer-sponsored retirement plan back into good standing may now be reduced.

EMPLOYMENT LAWSCENE ALERT: REMEMBER MARCH 1 DEADLINE FOR REPORTING A "SMALL" HIPAA BREACH

Employers who are classified as covered entities under HIPAA are required to report any 2018 breach of protected health information that affected fewer than 500 individuals (also known as a small breach) by March 1, 2019. This current breach notification requirement arises from amendments made to HIPAA under the Health Information Technology for Economic and Clinical Health (HITECH) Act, as finalized in 2013. HIPAA defines a covered entity as either (1) a group health plan, (2) a health care clearinghouse, or (3) a health care provider who electronically transmits any protected health information. A covered entity may be an individual, an institution, or an organization.

Background

Under applicable rules, a breach is defined as an impermissible use or disclosure under the HIPAA Privacy Rule that compromises the security or privacy of the protected health information. Some exceptions apply, so that not all incidents will rise to the level of a breach. Still, an impermissible use or disclosure of protected health information is generally presumed to be a breach unless the covered entity demonstrates that there is a low probability that the protected health information has been compromised based on a risk assessment of several specified factors.

Notification Requirement

Upon the occurrence of a confirmed (or in some cases, suspected) breach, the affected individuals must be provided with detailed notification letters without unreasonable delay and no later than 60 days after the discovery of the breach. While the covered entity, most often, provides the required notifications, the final rules permit the delegation of reporting duties to a business associate.

A HIPAA breach also triggers an obligation to notify the Office of Civil Rights (OCR) of the U.S. Department of Health and Human Services (HHS).

- When a breach affects 500 or more individuals, the reporting entity must notify OCR contemporaneously with the notification to individuals (and must also notify local media outlets).
- Where a breach affects fewer than 500 individuals (also known as a small breach), however, a reporting entity must maintain a log or other documentation of all breaches occurring during the year, and annually report all such breaches no later than 60 days after the end of that calendar year.

For a small breach occurring any time in 2018, the deadline to report that breach to OCR is March 1, 2019.

Small Breach Reporting Details

A reporting entity is not required to wait until the March 1 deadline to report a small breach. Small breaches may be reported as early as contemporaneously with the occurrence of the breach. Regardless of timing, all small breaches must be reported to OCR in the same manner. Specifically a reporting entity must report the breaches online through the OCR's "Breach Portal."

Note that even when a covered entity delegates the reporting function to a business associate, the covered entity retains ultimate legal responsibility for proper reporting. Accordingly, covered entities who delegate reporting may want to require proof of timely reporting.

Be aware that, while the reporting entity may report all small breaches on a single date, each separate breach incident will require a separate submission. Instead of simply uploading a log of breach incidents occurring in the prior year, the reporting entity must complete a six-section questionnaire to provide: (1) general information; (2) identification of the covered entity, business associate, and relevant contact information; (3) the nature of the breach; (4) a summary of related notices provided and actions taken; (5) an attestation, and; (6) a summary. Multiple fields must be completed within each of these six sections. The HIPAA status of a reporting party (as either a HIPAA covered entity or a business associate) must be indicated on the "Contact" tab of the online filing form.

The online reporting form also requires the reporting entity to indicate the level of pre-breach HIPAA compliance status, including whether or not HIPAA Privacy Rule safeguards and HIPAA Security Rule safeguards were in place.

Because filing the breach notice can be time-consuming, parties tasked with reporting 2018 small HIPAA breaches of unsecured protected health information are advised to gather and prepare the content to be reported before actually logging on to the OCR Breach Portal. Because any changes or updates to the submitted information must be entered as a separate entry, it is preferable to ensure that each submission is fully accurate. Moreover, because the content of Breach Notifications to OCR can form the basis for a future OCR investigation and enforcement action, it is advisable to have legal counsel review content prior to submission.

In addition to ensuring that 2018 breaches affecting fewer than 500 individuals are reported by March 1, covered entities and business associates should continue to ensure that HIPAA Policies and Procedures, as well as the applicable administrative, physical and technical safeguards are up to date and periodically reviewed.

EMPLOYMENT LAWSCENE ALERT: RECENT LEGISLATION IMPACTS QUALIFIED RETIREMENT

PLAN HARDSHIP WITHDRAWAL AND PLAN ROLLOVER RULES

The two-year budget agreement passed by Congress on Friday, February 9th, and signed by President Trump later that day, includes tax policy changes that affect qualified retirement plans. Specifically, qualified retirement plan hardship withdrawal operations will be impacted by the Bipartisan Budget Act of 2018 (the Budget Act) as follows:

- **Removal of the six-month prohibition on deferrals following a hardship withdrawal.** Section 41113 of the Budget Act directs the IRS to issue updated guidance to permit 401(k) and 403(b) plan participants who have taken a hardship distribution from a retirement plan to continue contributing to the plan, even immediately following the hardship distribution. Under current rules, once a participant elects to take a hardship distribution, no elective deferrals are permitted to be made until six months have passed from the date of the distribution. The revised rule will take effect on January 1, 2019 for plans that have a calendar-year plan year.
- **Inclusion of QNECs, QMACs, and profit-sharing contributions in hardship withdrawals.** Under current regulations, a plan sponsor may specify the sources of a participant's plan assets eligible for a hardship withdrawal, but such assets may in no event include certain employer contributions. Beginning on January 1, 2019 (for calendar-year plans), the Budget Act rules will permit a participant's 401(k) or 403(b) plan assets deriving from employer profit-sharing contributions, as well as from employer corrective contributions known as Qualified Nonelective Employer Contributions (QNECs) and Qualified Matching Contributions (QMACs), to be included in sources from which a hardship withdrawal may be taken. The earnings on such contributions will also be included among the assets available for withdrawal. Section 41114 of the Budget Act not only expands the potential sources of a hardship withdrawal, but also eliminates the requirement (previously elected by some employers) that a participant must have taken a plan loan before qualifying to take a hardship withdrawal.

The Tax Cuts and Jobs Act of 2017 (the Tax Act), signed into law by President Trump on December 22, 2017, affects certain plan loan distributions. Specifically, for all tax-qualified retirement plans that offer loans, including 401(k), 401(a), 403(b), and governmental 457(b) plans, the Tax Act provides for an:

- **Extended Deadline for Rolling Over Certain Plan Loan Offsets.**
    - Background and prior law: A plan loan "offset" occurs when an individual owes an outstanding loan to a qualified retirement plan, but then experiences a distribution event that is either (1) a termination of employment; or (2) the termination of the plan. If the plan, in such situation, permits a participant's account balance to be paid out in full, minus the loan amount, then a plan loan offset occurs. A Form 1099-R is issued, indicating that the offset amount is an actual distribution. If a participant receiving a loan offset takes no action, the offset loan amount is

considered or “deemed” to be a distribution, and is subject to taxation. Under these facts, taxation of the offset amount can be avoided if: (1) the distribution is otherwise eligible to be rolled over; and (2) the participant rolls the full amount of the distribution, including the amount of the offset, into an IRA. To include the offset amount in the rollover, the participant will need to contribute personal (or borrowed) funds to the rollover amount. Previously, offset loans could only avoid taxation if such a rollover occurred within the 60-day period beginning on the date offset distribution.
    - New law, effective for plan years beginning on and after January 1, 2018: The Tax Act expressly extends the time period for avoid taxation by rolling over an offset loan until the participant’s deadline for filing a federal income tax return (taking any extensions into account). This change means that in many cases, a participant will have more time in which to effect a tax-free rollover of a loan offset occurring following termination of employment.

Caution: No Change to Basic Tax Rules

Although recent legislation is trending toward easing the rules relating to hardship withdrawals and plan loans, it is important to remember that nothing about the fundamental tax treatment of these distributions have changed.

A common misconception (especially among participants) is that if a participant qualifies for a hardship distribution, then the distribution from the plan is tax-free.
A hardship distribution is subject to the same taxation rules as other plan distributions. Satisfying the standards for a hardship distribution simply entitles the participant to receive an in-service distribution of elective deferrals (and other contributions) from the plan, but the hardship distribution is subject to income taxes applicable to plan distributions. A hardship distribution is also generally subject to a 10% early distribution penalty, unless the participant has reached age 59-1/2. A hardship distribution is never eligible to be rolled over into an IRA.

Similarly, once a plan loan has been deemed distributed (either due to a plan loan repayment default, because a plan does not provide for an offset option upon distribution, or because an offset is not timely rolled into an IRA), the deemed distribution of a plan loan is taxed in the same manner as a regular plan distribution for purposes of determining the tax, including any early distribution penalty. A deemed distribution may never be rolled over into an IRA.

Plan Sponsor Action Items

With respect to plan hardship distributions, employer sponsors of 401(k) and 403(b) plans should prepare for the 2019 plan year by:

- Considering whether it is desirable to add a hardship distribution option to the plan (if not already permitted). If hardship distributions will be added, amend the plan and

communicate the availability of the option to participants by preparation and distribution of a Summary of Material Modification (SMM) (or other appropriate form of communication in the event of a non-ERISA plan).
- Plan documents that already provide for hardship distributions should be amended, effective for the first day of the 2019 plan year, to eliminate the 6-month restriction on elective deferrals following a hardship distribution and to expand the permitted accounts from which hardship distributions may be taken. These details should be communicated to participants in the form of an SMM.

With respect to plan loans, plan sponsors of plans that permit loans should:

- Review the plan loan policy and plan loan provisions to determine if either should be updated to reflect this rule, or consider whether to modify the loan policy to take advantage of this rule. For example, if the plan currently permits continued loan repayments following termination of employment consider whether this option should be continued or eliminated. Consider also whether a loan note should be allowed to be rolled over to a successor plan upon plan termination or if the new extended rollover period provides sufficient flexibility to participants absent a rolled over loan note.
- Consider whether plan participant communications should be revised to alert participants to the greater flexibility now allowable for rollover of loan offset amounts.
- As applicable, confer with any third-party administrator for the plan to avoid inadvertently deeming a participant’s loan a deemed (taxable) distribution.