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Employee Benefit Plan Review

Ask the Experts

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Responsibility for COBRA Continuation Coverage in M&A Transaction

Q My company is a parent company with three related subsidiaries. We sponsor one group health plan covering all four entities. We are negotiating the sale of one of our subsidiaries to a potential buyer that has its own group health plan. There are a number of individuals on COBRA continuation coverage on our health plan, many of whom previously worked for the subsidiary that we are trying to sell. Who will be responsible for the COBRA continuation coverage of these individuals after the sale?

A Ultimately, your company will retain responsibility for COBRA continuation coverage, but you could negotiate the purchase agreement to require the buyer to assume responsibility for such COBRA continuation coverage. Under the applicable COBRA regulations, in general, as long as your company maintains a group health plan after the sale, then your company's group health plan will have the obligation to provide COBRA coverage to qualified beneficiaries whose qualifying event occurred prior to or in connection with the sale, or a covered employee whose last employment prior to the qualifying event was with your company (M&A Qualified Beneficiaries.) However, the COBRA regulations permit the seller and the buyer to allocate the responsibility to provide COBRA coverage differently in a purchase agreement. As a result, you may want to try to negotiate as a condition of the sale of your subsidiary that the buyer assume responsibility for COBRA coverage of M&A Qualified Beneficiaries under their group health plan. Whether the buyer is willing or able to assume this responsibility will depend on several factors, including whether the buyer is able to secure or provide coverage under its plan or another plan within its controlled group of corporations. In some cases, a buyer may only be willing to agree to use commercially reasonable efforts to provide such coverage, but may not guarantee providing such coverage. If the buyer does agree to assume responsibility for such continuation of coverage but fails to perform, your company's group health plan will continue to have the obligation to make COBRA continuation coverage available to the M&A Qualified Beneficiaries. For these reasons, it is important to include specific provisions in the purchase agreement regarding the allocation of responsibility in connection with the sale, the efforts that must be made by the buyer to provide such continued coverage, and any financial or other remedy that would occur if the buyer fails to provide such continued coverage.

For more information, *see* Treas. Reg. § 54.4980B-9.

Providing Form W-2 To Employees with Minimal Compensation

Q Last year, my company employed a large number of part-time and short-term workers who, in some cases, earned less than $500 total from the company. Is there a de minimis exception to the Form W-2 requirement which would exempt us from the requirement to issue Form W-2s for such employees?

A In general, your company must complete and issue a Form W-2 for each employee for whom any of the following applies: (1) your company withheld any income, social security, or Medicare tax from wages regardless of the amount of wages, (2) your company would have had to withhold income tax if the employee had claimed no more than one withholding allowance or had not claimed exemption from withholding on Form W-4; *or* (3) your company paid $600 or more in wages even if you did not withhold any income, social security, or Medicare tax. There is no general "de minimis" exception from the W-2 requirement for employees who received only a certain minimal amount of compensation from your company. There is, however, a very limited exception to the requirement to issue a Form W-2 which applies if your company was not required to withhold *any* income tax, social security tax, or Medicare tax, *and* your company was required to pay the employee less than $600.

For more information, *see* Treas. Reg. § 31.6051-1 and IRS General Instructions for Forms W-2 and W-3.

Simple Employee Plan Eligibility

Q I own a small business and am thinking about setting up a Simplified Employee Pension Plan for my employees. I understand that employees are required to meet certain eligibility requirements, including being at least age 21 and working for my business for at least three years. Is there any way that we could waive the three-year requirement and allow employees who have less than three years of service to join the SEP either immediately or after six months of service?

A Yes, the rules governing Simplified Employee Pension (SEP) plans require that all employees who have met all three of the following requirements be permitted to participate in the SEP:

- *Age*: Employees who have attained age 21;
- *Service*: Employees who have worked for the employer during any period in each of three out of the last five plan years (sometimes referred to as the "3 of 5" rule); and
- *Compensation*: Employees who received at least $600 in compensation from the employer for the year.

In addition, employees who are covered under a collective bargaining agreement pursuant to which retirement benefits were the subject of good faith bargaining and employees who have no U.S. source income may be excluded from a SEP.

These rules are intended to set the outside limits on who may be excluded from a SEP. Employers may choose to permit employees who are younger than age 21, who have worked less than three out of the last five years and/or who earn less than $600 in compensation to participate in a SEP. As a result, you may permit employees to participate immediately or wait six months before joining your SEP.

If you do decide to require that employees work at least three out of the last five plan years, you would need to count any service (*e.g.*, one day, one month) that the employee worked in any of the five plan years immediately preceding the year for which a SEP contribution would be made. For example, if your plan year is the calendar year, in determining whether an employee is eligible for a SEP contribution for the year 2019, an employee who worked during any period in at least three out of the immediately preceding five calendar years (2014 through 2018) would be eligible for a 2019 contribution (assuming the employee met the minimum service and compensation requirements, if you choose to impose those).

In establishing a SEP, it is helpful to consult with a qualified tax advisor who is familiar with SEP requirements. It is also important to review the SEP documents to ensure that they reflect the provisions that you would like to include and to have procedures in place to ensure that the SEP is being operated in accordance with the terms you have chosen and the IRS rules.

For more information on establishing a SEP, *see https://www.irs.gov/retirement-plans/retirement-plans-faqs-regarding-seps-establish-a-sep*.

Simple Employee Pension Plan Contributions

Q My company has a SEP that requires each employee to earn at least $600 in a plan year to be eligible to receive a SEP contribution. In calculating the SEP contribution, do we count only the compensation received after the employee earned the $600 or all of the employee's compensation for the plan year?

A IRS rules require that, once the employee has earned the $600 and met any other permissible minimum eligibility requirements, you count all of the employee's compensation earned for the plan year.

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