VOLUME 74 ◆ NUMBER 4

Employee Benefit Plan Review

Ask the Experts

By Marjorie M. Glover, David Gallai, and Rachel M. Kurth

Pension Plan Relief

Q Can you explain the relief provided to traditional pension plans in the recently passed CARES Act?

A There are a couple of provisions in the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") that directly apply to traditional pension plans (also referred to as single-employer defined benefit pension plans).

First, in order to permit increased cash liquidity for plan sponsors in the short-term, any required minimum funding contributions to the plan that would otherwise be due during 2020 is now not due until January 1, 2021. However, any contributions to the plan that are delayed under this relief provision must be increased to account for interest (at the plan's effective rate of interest) for the period of time between the original due date of the contribution and the actual date on which the contribution is made.

Second, for purposes of calculating a pension plan's AFTAP for the plan year or years that include 2020 (AFTAP is the acronym for a plan's "adjusted funding target attainment percentage"), instead of calculating the actual AFTAP for that plan year, a plan may use the AFTAP for the most recent plan year ending before January 1, 2020. Given the market turmoil caused by the COVID-19 pandemic, actual AFTAPs for most plans for 2020 are expected to decrease, in some cases significantly. Decreased AFTAPs could result in pension plans having to apply certain benefit restrictions under the plan (such as limiting lump-sum distributions). To avoid such results based on the sudden market decrease caused by the COVID-19 economic shutdowns, plan sponsors can rely on this relief in the short-term.

Finally, while not contained in the CARES Act, under the Pension Benefit Guaranty Corporation's ("PBGC's") existing disaster relief guidance, certain filing deadlines and premium payment deadlines have been extended until July 15, 2020 (subject to potentially further extension). For further information about this disaster relief, see the PBGC's press release number 20-02 (issued on April 10, 2020) and the guidance links contained within that press release.

Expanded FMLA Leave That Must Be Paid

Q My company has about 150 employees and we have always offered eligible employees leave under the Family and Medical Leave Act ("FMLA") for FMLA-qualifying reasons, such as leave related to a serious health condition or an employee's new child. We have always offered FMLA leave as unpaid leave. I heard that there is a new law that expands FMLA leave to cover certain reasons related to the novel coronavirus that causes COVID-19, and further, that this new expanded FMLA leave must be paid. Does this new law mean that my company now has to pay employees when they are out on any type of FMLA leave?

A No. You are correct that there is a new law that creates a new category of FMLA leave. That law is the Families First Coronavirus Response Act ("FFCRA"), which went into effect on April 1, 2020 and will only be in effect through December 31, 2020. That law has two aspects that generally apply to private employers with fewer than 500 employees. One aspect of the FFCRA, the Emergency Paid Sick Leave Act ("EPSLA"), provides up to two weeks of paid or partially paid sick leave where an employee is unable to work for certain reasons related to COVID-19.

The other aspect of the FFCRA, which you referenced in your question, is the Emergency Family and Medical Leave Expansion Act ("EFMLA"), which creates an expanded FMLA leave right for an eligible employee who is unable to work (or telework) due to a need to care for his or her child whose school or place of care has been closed, or whose child care provider is unavailable, for reasons related to COVID-19.

Eligible employees will have up to 12 weeks of EFMLA leave to use from April 1, 2020 through December 31, 2020, which time is included in and not in addition to the total FMLA leave entitlement of 12 weeks in a 12-month period under the existing FMLA rules. EFMLA leave can be unpaid for the first two weeks of EFMLA leave unless an employee qualifies to use, and uses, paid leave provided under the EPSLA during this time.

After the first two weeks of EFMLA leave, employers must pay an employee on EFMLA leave at two-thirds of the employee's average regular rate of pay for the number of hours that the employee would otherwise normally be scheduled to work during the period of such leave. EFMLA leave pay is capped at $200 per day and $10,000 in total, or $12,000 in total if using EPSLA leave during the first two weeks of EFMLA leave.

After the first two weeks of EFMLA leave, an eligible employee may elect, or your company may require, that the employee take the remaining EMFLA leave at the same time as any existing paid leave that, under your company's policies, would be available to the employee in that circumstance. Note that EFMLA leave is the only type of FMLA leave that is now required to be partially paid. The type of FMLA leave that is now partially paid applies only to leave taken because an employee must care for a child whose school or place of care has closed, or whose childcare provider is unavailable, for reasons related to COVID-19.

Paid leave is still not required for any other type of FMLA leave. Your company generally would qualify for dollar-for-dollar reimbursement through tax credits for all qualifying wages paid under the FFCRA. Qualifying wages are those paid to an employee who takes leave under the FFCRA for a qualifying reason, up to the appropriate per diem and aggregate payment caps. Applicable tax credits also extend to amounts paid or incurred to maintain an employee's health insurance during qualifying leaves. Your company may choose to pay your employees in excess of the FFCRA's paid leave requirements, but your company would not be able to receive tax credits for amounts in excess of the FFCRA's statutory limits.

New Plan Withdrawal Provisions

Q My company sponsors a 401(k) plan for our employees. I have read that the new COVID-19 legislation allows employees to withdraw amounts from 401(k) plans. Are these withdrawal provisions required or optional? What is the deadline for amending our 401(k) plan to provide for these withdrawals?

A Under the CARES Act, plan sponsors of tax-qualified plans, including 401(k), 403(b), and 457 plans, may permit eligible individuals to receive certain "coronavirus-related distributions." These distribution provisions are optional and not mandatory.

An eligible individual is an individual who:

- Is diagnosed with COVID-19;
- Has a spouse or dependent who is diagnosed with COVID-19; or
- Experiences adverse financial consequences as a result of being quarantined, furloughed, laid off, having work hours reduced, being unable to work due to lack of childcare due to COVID-19, closing or reducing hours of a business owned or operated by the individual due to COVID-19, or other factors as determined by the Treasury Secretary.

Under the CARES Act, eligible individuals may receive qualifying coronavirus-related distributions of up to $100,000 from the eligible individual's individual retirement arrangements and tax-qualified plans that permit such withdrawals, without incurring a 10 percent penalty tax that may otherwise apply to distributions received prior to attainment of age 59 1/2. The $100,000 limit applies to all tax-qualified plans of the employer and any related employers (applying the controlled group rules of Internal Revenue Code Section 414). Qualifying coronavirus-related distributions may be made by employees who are still working or on leave. Plan sponsors may rely upon participant certifications that the participant is an eligible individual who has incurred a qualifying coronavirus-related event.

Qualifying coronavirus-related distributions are limited to distributions made from January 1, 2020 through December 31, 2020. The income attributable to such distributions would be taxable over a three-year period. Participants are also permitted to recontribute the distributed funds to an eligible retirement plan within the three-year period, without regard to the annual limitations on contributions that would normally apply. In addition, coronavirus-related distributions are not subject to the mandatory 20 percent federal income tax withholding that would normally apply.

Although a plan sponsor may choose to make coronavirus-related distributions available now, the deadline for formally amending a tax-qualified plan to provide for coronavirus-related distributions is the last day of the first plan year beginning on or after January 1, 2022. If your company's 401(k) plan has a calendar year plan year, and your company chooses to offer coronavirus-related distributions, the deadline for amending your company's 401(k) plan would be December 31, 2022. It is possible that the Internal Revenue Service may delay the amendment deadline further.

Finally, we note that in addition to the special coronavirus-related distribution options, the CARES Act provides additional relief for plan loans and required minimum distributions.

401(k) Distributions Upon Sale Of Business

Q We sponsor a 401(k) plan and are considering selling one of our subsidiary business units. If we sell a business unit, at the time of the sale, can we distribute the 401(k) plan accounts to employees who want to take their money out of the plan? Does it matter if the sale of the business unit is an asset sale or a stock sale?

A The answer to this question will depend on who sponsors the 401(k) plan and how the 401(k) plan is handled as part of the sale of the business unit. Under the Internal Revenue Service ("IRS") regulations for 401(k) plans, elective employee deferrals to a 401(k) plan may not be distributed before a distributable event occurs. One such distributable event is a severance from employment. Severance from employment is defined as ceasing to be an employee of the employer maintaining the plan.

So, if your 401(k) plan is maintained at the parent entity level, then employees employed by the subsidiary that is sold (whether via a stock sale or an asset sale, assuming that the employees do not remain employed with the seller or its affiliates) will be deemed to have had a severance from employment, and may elect to take a distribution from the 401(k) plan after the sale.

However, if the buyer maintains your company's 401(k) plan, either because it assumes sponsorship of the plan as part of the transaction (for example, if the 401(k) plan is maintained by the sold subsidiary and the transaction is a stock deal) or it accepts a transfer of plan assets and liabilities into its own 401(k) plan as part of the transaction, then employees of the sold subsidiary who continue to be employed by the buyer after the sale will not be deemed to have had a severance from employment.

As an aside, you may be interested in knowing that this rule used to be different, and more difficult for parties to a corporate transaction to agree upon and apply. The prior rule, referred to as the "same desk" rule, basically said that an employee did not have a separation of service, and therefore could not take a distribution of their 401(k) plan account, if they continued to do the same job (that is, do the same work from their "same desk") after the transaction unless certain conditions were met. The "same desk" rule was repealed and replaced in 2002 by the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA").

Severance Plans and ERISA

Q What are the benefits of subjecting our discretionary severance policy to ERISA?

A The Employee Retirement Income Security Act of 1974 ("ERISA") governs welfare benefit plans. Severance arrangements are one type of welfare benefit plan that may be subject to ERISA. While your business may elect to voluntarily subject your severance policy to ERISA, ERISA may still apply to your policy even if you prefer that it not apply.

There is much case law on what types of severance arrangements are subject to ERISA, all of which is basically derivative of the U.S. Supreme Court's 1987 decision in *Fort Halifax Packing Co., Inc. v. Coyne*. Essentially, the questions are whether a business has an ongoing severance arrangement that extends beyond a single event and what level of employer administration is required to maintain the arrangement. There are a number of factors the fall under the umbrella of these questions. All of this is simply to say that your business' severance policy may already be subject to ERISA.

In terms of the benefits of ERISA coverage, there are many, three of which follow.

First, ERISA is a federal law that generally pre-empts state law. As such, many state law claims that a participant in a severance plan might otherwise be able to bring against your business will be pre-empted. This could be particularly helpful for a business that has employees in multiple states with differing laws governing wages and related matters.

Second, ERISA requires that severance plans have a claims and appeals procedure. A participant is required to utilize these procedures before commencing litigation under the plan. And once litigation is commenced, if the severance plan is drafted properly, courts will generally be required to provide a good deal of deference to the plan administrator's conclusion. Put simply, this claims and appeals procedure helps to insulate the plan administrator's decisions under the plan from second guessing by courts.

Third, in the event there is litigation, ERISA claims do not provide for jury trials. A judge would typically decide the ERISA claim, which is generally viewed as more favorable for plan sponsors.

Finally, please keep in mind that severance arrangements that are subject to ERISA have certain obligations under ERISA that must be complied with. While these obligations are generally not onerous, penalties can become expensive if they are not complied with. Most prominently, ERISA plans must be set forth in a formal plan document and have a summary plan description. Severance plans often have a single document that acts as both the severance plan and the summary plan description. Also, if the severance plan covers enough employees (100 or more), the plan must file an annual return with the Department of Labor (known as the Form 5500).

Marjorie M. Glover, a partner in the New York City office of Norton Rose Fulbright US LLP, focuses her practice on executive compensation and employee benefits law, corporate governance and risk oversight and employment law. David Gallai, who also is a partner in the firm's New York City office, practices in the areas of employment counseling, executive compensation, and employee benefits. Rachel M. Kurth is a senior counsel at the firm. They can be reached at *marjorie.glover@nortonrosefulbright.com*, *david.gallai@nortonrosefulbright.com*, and *rachel.kurth@nortonrosefulbright.com*, respectively.