



Recent Developments Affecting Retirement and Welfare Plans and Executive Compensation

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What We Intend to Cover



■ Leigh Riley

- Qualified Retirement Plans

■ Nick Welle

- Health and Welfare Plans

■ Joshua Agen

- Equity Incentive Plan Updates
- Future of CEO Pay Ratio and Other Dodd-Frank Rules



Qualified Retirement Plans

No More Determination Letters



- **Two types of plan documents:**
 - Off the shelf (prototype and volume submitter)
 - Individually designed
- **Off the shelf plans could get IRS opinion letter every 6 years**
- **Individually designed plans (IDPs) could obtain IRS favorable determination letter every 5 years**

No More Determination Letters



- **No changes to off the shelf plans**
 - Vendor will continue to submit blank form to IRS for approval
 - Employers will then need to adopt approved plan after vendor gets IRS letter
- **As of January 31, 2017, no more determination letters for IDPs**
 - Other than new plan or terminating plan

New Annual Amendment List



- **IRS proposed new annual process to help IDPs ensure document compliance**
- **Annual Required Amendments List**
 - Must be adopted within two calendar years (unless IRS says otherwise)
 - Amendments on 2016 List adopted by December 31, 2018 (but may have retroactive effective date)
- **2016 Amendment List – one minor change for collectively bargained pension plans to AFTAP language**

What to Do?



- **Consider moving from IDP to off the shelf, if feasible**
- **Strictly follow the IRS amendment list (even if amendment may not necessarily be needed)**
- **Be prepared for auditors' questions**

Enhanced Rollover Rights



Two rollover types:

- Direct rollover (check made payable to plan)
- Indirect rollover
 - Payable to participant minus 20%
 - 60 days to deliver check (with 20% if desired) to new plan

Enhanced Rollover Rights



- Participants who missed the 60-day deadline could ask IRS for waiver
- IRS now granted “blanket waiver”
 - Rev. Proc. 2016-47
- Self-certification procedures

Self-Certification



- **60-day deadline missed due to specified list, such as:**
 - Financial institution error
 - Misplaced check
 - Death or illness in family
- **IRS had not previously denied waiver for same rollover amount**
- **Rollover accomplished as soon as possible**

Effect on Plan



- **Plan can rely on self-certification and accept rollover**
 - Unless have actual knowledge of false statement

Plan amendment may be needed; issue SMM

Coordinate with recordkeeper


Use model certification found in IRS Rev. Proc.

Safe Harbor 401(k) Plans



- Two types of safe harbor designs:
 - Traditional: employer safe harbor contributions fully vested
 - QACA: vesting schedule OK
- Forfeitures now may be used to pay “traditional” safe harbor employer contributions (Fed. Reg. Jan. 18, 2017)
- Plan amendment likely needed


Mid-Year Changes to Safe Harbor Plans



Expanded mid-year amendments: IRS Notice 2016-16

- Previously, generally prohibited
- Can make any change now, unless prohibited (see next slides)
- If it affects safe harbor notice, revised notice provided 30 days in advance of change

What is prohibited?

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- Increase # of years needed to vest (QACA)
 - Remove employees from eligibility (but only if already eligible)
 - Change type of safe harbor plan
 - Increase matching formula or add discretionary match unless:
 - Adopted at least 3 months before plan year end,
 - Retroactively applies for the entire plan year, and
 - Updated safe harbor notice and election opportunities provided at least 3 months prior to plan year end.

Also prohibited



- **Stopping safe harbor contributions mid-year**
- **Start safe harbor status mid-year**

Separate rules apply to those

Examples of Permitted Changes



Increase future safe harbor non-elective contributions from 3% to 4% for all eligible employees

Add an age 59½ in-service withdrawal feature

Change the plan's default investment fund

Alter the plan rules on arbitration of disputes

Shift plan entry date from monthly to quarterly

Adopt amendments required by applicable law (for example, statutory law changes or court decisions)



Health & Welfare Plans

The Big Ten



- 1. 2017 Health & Welfare Numbers**
- 2. New SBC Template**
- 3. New Required Preventive Services**
- 4. Reinsurance & PCORI Fees**
- 5. Cures Act – Small Employer HRAs**
- 6. ACA Tax Reporting Extensions**
- 7. Final Disability Claims Procedure Regulations**
- 8. ADA Wellness Notice & GINA Authorization**
- 9. Section 1557 – Gender Reassignment & RDS**
- 10. Washington D.C. Update**

2017 Numbers



- HSA Contribution - \$3,400/\$6,750
- Health FSA - \$2,600
- HDHP OOPM - \$6,550/\$13,100
- ACA OOPM - \$7,150/\$14,300

New SBC Template



- **For Open Enrollments on or after April 1, 2017**
- **New template largely unchanged**
- **Notable Modifications:**
 - Add third coverage example
 - Revised COBRA, MEC, and MV language
 - Reduces from 8 to 5 pages

New Required Preventive Services



- **Plans on or after December 20, 2017**
 - January 1, 2018 for CY Plans
- **Updated Women's Preventive Services Guidelines**
 - Breastfeeding services and supplies
 - Well-woman preventive visits
 - Cervical cancer screenings

Reinsurance & PCORI Fees



■ Reinsurance Fees (\$27)

- If paid in one lump sum, you are all done!
- If paid in two installments, second portion (\$5.40) due November 15, 2017

■ PCORI Fees (\$2.17)

- Until 2019, but much smaller (minor increases)
- Due July 31 of each year

21st Century Cures Act



- **Small employers may now reimburse employees' premiums for individual coverage**
- **Conditions:**
 - Available to all employees, with some exceptions
 - Cannot exceed \$4,950/\$10,000
 - Same amount for all eligible employees, with exceptions for age and enrollee count
 - Distribute annual notice

ACA Tax Reporting

■ Extension for employee statements (1095-C)

	Original Deadline	Extended Deadline
Furnishing Form 1095-C to Employees	January 31, 2017	March 2, 2017
Filing Paper Forms 1095-C with IRS	February 28, 2017	No Extension
Electronically Filing Forms 1095-C with IRS	March 31, 2017	No Extension

■ No extension for filing with IRS

■ Extend good faith standard

Final Disability Claims Procedure Regulations



- **Effective January 1, 2018**
- **Mirror enhanced claims and appeals procedures for GHPs added by PPACA**
- **Notable Changes**
 - **Must explain disagreement with SSA, treating physicians, and medical/vocational experts**
 - **Must even explain why disagreed with expert obtained but not relied upon for the denial**
 - **Must include time limit to sue found in plan document**

ADA/GINA Wellness Rules



- **New notice requirement eff. January 1, 2017**
- **Lower Incentive Cap – 30% self-only (always)**
 - Applies only to disability-related inquiries and medical examinations
- **GINA Authorization**
 - Need for spousal participation in HRA

Section 1557 - Gender Reassignment Services & Retiree Health



- **Effective January 1, 2017, if receive RDS:**
 - No blanket exclusion for gender transition services
 - Cannot deny coverage because of transgender status
- **Injunction – Not Required to Comply Currently**
 - Unless another ruling, HHS banned from enforcing
- **Might have to apply if receive federal contract**

Health Care Reform Under New Administration



- No one knows for sure
- No real changes to ACA yet
- No uniform GOP direction for repeal and replace

What Has Happened Already



- **President Trump's ACA Executive Order**
 - Agencies to exercise their discretion to minimize the economic burdens of the ACA

GOP Statements on Repeal & Replace



■ Inconsistent

- Repeal then work on replace
- Both immediately and simultaneously
- As late as 2018
- Piecemeal fashion
- “Repair” ACA

Current Activity



■ Repeal by Budget Reconciliation

- Only ACA provisions relating to government spending and taxes
 - Employer mandate
 - Cadillac Tax
- Simple majority only (51 votes; 52 GOP Senators)
- Immune from filibuster

■ Possible Delay in Implementation

- Loss of coverage and market disruption concerns

GOP Proposals for Repeal & Replace



- 8 to 11 GOP proposals
- More to come
- No overwhelming support for one proposal



Equity Incentive Plan Updates

Equity Incentive Plan Updates - Overview



- Share withholding
- Director award limits
- ISS policy changes

Share Withholding in Equity Plans

- In 2016, the Financial Accounting Standards Board (FASB) amended ASC Topic 718 to simplify the accounting standards for stock-based compensation
- Before the amendment: Plans were required to limit share withholding to the minimum required withholding to avoid variable accounting
- After the amendment: Plans are permitted to allow share withholding up to the maximum statutory withholding requirement while still avoiding variable accounting

Share Withholding in Equity Plans

- Many companies are amending their equity plans to allow the plan administrator discretion to withhold shares up to the maximum statutory withholding requirement
 - Note that IRS rules on withholding still apply and were not changed by the amendment to the accounting rules
 - To apply the change to currently outstanding awards, award agreement amendments may also be needed
- NYSE and Nasdaq have provided guidance indicating this plan amendment does not require shareholder approval

Director Award Limits in Equity Plans

- Director pay, as well as executive pay, has been the subject of shareholder litigation
- *Calma v. Templeton (the “Citrix” case)*
 - In April 2015, the Delaware Court of Chancery Court refused to dismiss a breach of fiduciary duty claim brought by shareholders against the Board of Directors arising from equity compensation awards that Citrix Systems, Inc. had granted to its non-employee directors
 - The fact that Citrix’s shareholders had approved individual award limits in the equity plan under which the directors’ awards were granted did not secure business-judgment-rule deference with respect to the amount of the director pay because the limits in the plan were not “meaningful”
 - Instead, director defendants would have to show that their compensation was “entirely fair”

Director Award Limits in Equity Plans

■ Citrix settlement approved in 2016

– Company agreed to:

- Amend omnibus plan to limit annual equity compensation grants for non-employee directors (\$795,000, which is 2-3x historical or actual award amounts) and specify terms
- Submit amendments to shareholder approval
- Provide enhanced disclosures on director compensation practices
- Amend compensation committee charter to specify duties relating to director compensation

– Company paid \$425,000 in legal fees and expenses to plaintiffs' counsel

Director Award Limits in Equity Plans

- Other recent cases similar to Citrix
 - *Espinoza v. Zuckerberg, et al.*, filed in 2014 against the officers and directors of Facebook
 - Alleged directors received excessive compensation
 - Settled in 2016, with Facebook agreeing to make corporate governance reforms, submit director pay to a shareholder vote and pay up to \$525,000 in attorneys' fees and expenses to plaintiff
 - The Facebook complaint followed a 2012 Delaware case, *Seinfeld v. Slager*, which likewise alleged that directors had paid themselves excessive compensation
 - The court allowed plaintiffs to proceed without making a demand because the directors were not considered disinterested
 - Parties later settled
- **Recommendation:** Consider establishing separate, “meaningful” award limits for non-employee directors in shareholder-approved omnibus plans or using a separate shareholder-approved plan for awards to non-employee directors

ISS Policy Changes Affecting Equity Plans



- **ISS made two key changes to its “Equity Plan Scorecard” for 2017**
- **Minimum vesting period factor**
 - To receive full credit for this factor, an equity plan must specify a minimum vesting period of at least one year for all award types
 - Cannot be overridden in individual award agreements

ISS Policy Changes Affecting Equity Plans

■ Dividends and Dividend Equivalents

- New factor in the scorecard relating to whether dividends or dividend equivalents are payable prior to the vesting of the underlying equity award
- To get full credit, plan must explicitly prohibit the payment of all dividends or dividend equivalents before the vesting of the equity award
 - No credit if the prohibition is absent or incomplete
- To be “complete,” the prohibition must apply to all types of awards
- Accruing dividends or dividend equivalent units payable upon vesting is allowed so long as the dividends are withheld during the vesting period


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Future of CEO Pay Ratio and Other Dodd-Frank Rules

CEO Pay Ratio

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- Final rules are effective
 - First disclosures will be required in 2018 proxy statements
 - Pending legislation (the “Financial CHOICE Act”) would repeal the Dodd-Frank mandate if enacted
 - Legislation may not become effective until late in 2017 or in 2018, and SEC could still require the ratio on the basis of other statutory authority
 - However, acting SEC Chair Piovolar has announced reconsideration of implementation and is seeking comments
 - **Recommendation:** Do at least enough groundwork to determine how much ramp-up time would be needed to comply if the rule remains, but otherwise monitor for further developments

SEC Staff Compliance and Disclosure Interpretations (Oct 2016)

- Pay measure used to identify median employee must “reasonably reflect annual compensation” but need not identify the same median employee as using annual total compensation
- Relying exclusively on hourly or annual rates of pay not permissible
- Time period used need not be annual or include employee determination date
 - Can be prior fiscal year (at least if annual total compensation is used)
- Whether furloughed employees must be included depends on facts and circumstances
- Registrant is not considered to determine the compensation of independent contractor or leased worker if it obtains their services by contracting with an unaffiliated third party that employs the worker

Compensation Clawback



- Rules were proposed but have not been finalized
- Pending CHOICE Act would narrow (but not repeal) the Dodd-Frank requirements if enacted
 - Clawback would apply only to executives who had “control or authority” over financial statements
- Many companies have already adopted clawbacks voluntarily and may continue to maintain them because of popularity with investors

Disclosure of Pay Versus Performance



- Rules were proposed but have not been finalized
- Not covered by CHOICE Act, but other legislation could repeal
- At a minimum, this requirement probably will not be effective for some time

Disclosure Whether Hedging Transactions are Permitted



- Rules were proposed but have not been finalized
- CHOICE Act would repeal
- Many companies have voluntarily prohibited hedging and will likely continue to do so given popularity with investors

Say on Pay



- **CHOICE Act would change required frequency from every one, two or three years to “each year in which there has been a material change to the compensation”**
- **May not affect practice**
 - Unclear at this stage what would constitute a “material change” triggering a vote
 - Institutional investors and companies are generally accustomed to annual votes

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