ERISA Newsletter

First Quarter 2017

A report to clients and friends of the firm

Edited by Stacey C.S. Cerrone and Russell L. Hirschhorn

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Editor's Overview

After a brief hiatus, Proskauer's ERISA Newsletter is back with a brand new look. We hope you like it and find it is easier to navigate. In addition to implementing our new format, we have moved to a quarterly publication with publication dates in January, April, July and October. You also will find a compilation of our Employee Benefits & Executive Compensation Blog over the past quarter organized by topics in this publication.

This quarter's featured article takes a look at employer stock fund claims based on inside information in a post-*Dudenhoeffer* world. The courts' application of *Fifth Third Bancorp v. Dudenhoeffer* has resulted in substantial hurdles for the plaintiffs' bar to get past the motion to dismiss stage. Whatever happiness plaintiffs may have first felt when the Supreme Court tossed out the presumption of prudence has likely dissipated in the wake of the lower courts' subsequent application of *Dudenhoeffer*. Is the subsequent decline in new employer stock suits a result of that mood change, or just a necessary consequence of the bull market?

Courts Close Their Doors to ERISA Stock-Drop Litigation*

By Joe Clark

It has been almost three years since the U.S. Supreme Court, in *Fifth Third Bancorp v. Dudenhoeffer*, 134 S. Ct. 2459 (2014), established new pleading standards for plaintiffs alleging that 401(k) plan fiduciaries breached their ERISA fiduciary duties by continuing to allow plan participants to invest in employer stock. In the immediate aftermath of *Dudenhoeffer*, the plaintiffs' bar hailed the decision as a victory, claiming that without the "presumption of prudence" under which stock-drop claims had been evaluated for the past two decades, participants would finally be able to have their claims adjudicated on their merits. But plaintiffs' elation with *Dudenhoeffer*'s rulings was short-lived. The removal of the presumption of prudence was accompanied by the Court's articulation of new pleading requirements that were intended as a means of "dividing the plausible sheep from the meritless goats." These newly articulated standards have generated results not dissimilar from those experienced before *Dudenhoeffer*.

In an earlier article, we observed that stock-drop claims based on public information face significant difficulties at the pleadings stage. The same now appears to be true for stock-drop claims based on inside information. As discussed below, since *Dudenhoeffer*, courts have routinely dismissed such claims on motions to dismiss.

The Supreme Court's Decisions in *Dudenhoeffer* and *Amgen*

In *Dudenhoeffer*, the Supreme Court set forth the pleading standards applicable to ERISA fiduciary breach claims challenging employer stock investments in 401(k) plans. The Court developed a two-prong test to state a plausible claim for breach of fiduciary duty based on insider information. Under that test, a plaintiff must plausibly allege "an alternative action that the defendant could have taken that [1] would have been consistent with the securities laws and [2] that a prudent fiduciary in the same circumstances would not have viewed as more likely to harm the fund than to help it." 134 S. Ct at 2472.

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The Supreme Court emphasized that courts adjudicating such claims must undergo the "important task" of weeding out meritless claims by engaging in "careful, context-sensitive scrutiny of a complaint's allegations." Id. at 2470. Anticipating that participants, like the plaintiffs in that case, would seek to meet their burden by proposing that defendants halt all purchases of company stock or publicly disclose insider information to cure the alleged artificial inflation in employer stock price, the Court stressed that:

> lower courts faced with such claims should also consider whether the complaint has plausibly alleged that a prudent fiduciary in the defendant's position could not have concluded that stopping purchases – which the market might take as a sign that insider fiduciaries viewed the employer's stock as a bad investment – or publicly disclosing negative information would do more harm than good to the fund by causing a drop in the stock price and a concomitant drop in the value of the stock already held by the fund.

Id. at 2473

Two years later, the Supreme Court reconfirmed that this test must be applied rigorously at the pleadings stage. In *Amgen, Inc. v. Harris*, 136 S. Ct. 758, 760 (2016), the Court summarily reversed the Ninth Circuit's decision permitting an employer stock claim to proceed because the Ninth Circuit had failed to determine whether the complaint plausibly alleged that removal of the Amgen stock fund from the list of investment options was an action that a prudent fiduciary could not have concluded would "do more harm than good."

In complaints filed after *Dudenhoeffer* that alleged claims based on insider information, plaintiffs have sought to satisfy *Dudenhoeffer's* pleading standard by proffering a variety of courses of actions that they contended no prudent fiduciary in similar circumstances could have concluded would do more harm than good, including: (i) freezing purchases and sales of employer stock; (ii) publicly disclosing unfavorable inside information about the company; and (iii) seeking guidance from the Securities and Exchange Commission (SEC) or DOL. Time after time, courts have rejected these proposed alternatives.

Freezing Purchases and Sales of Employer Stock

Defendants have long argued that selling or liquidating employer stock holdings on the basis of inside information was not a viable option because it would violate the securities laws. The SEC agreed in an amicus brief, but also stated that freezing purchases and sales of employer stock would not violate the securities laws. The DOL stated in a companion amicus brief that a plan fiduciary could prevent the plan from purchasing overvalued stock by freezing purchases and sales of employer stock.

The plaintiffs' bar, unsurprisingly, frequently has argued that plan fiduciaries with knowledge of unfavorable inside information should have frozen purchases and sales of company stock until the stock was no longer an imprudent investment. But the courts have repeatedly held that this proffered course of action failed to satisfy the second prong of *Dudenhoeffer*'s test—namely, that no prudent fiduciary could conclude that the proffered course of action would cause more harm than good. In some cases, the courts have found plaintiffs' assertion failed to meet the pleading requirements because it was too conclusory. See *Whitley v. BP, P.L.C.*, 838 F.3d 523, 529 (5th Cir. 2016) ("Aside from these conclusory statements, the stockholders do not specifically allege, for each proposed alternative, that a prudent fiduciary could not have concluded that the alternative would do more harm than good, nor do they offer facts that would support such an allegation."); *Martone v. Whole Foods* (W.D. Tex. Sept. 28, 2016) (same); *Wilson v. Edison International, Inc.* (C.D. Cal. July 6, 2016) ("[T]he Complaint makes conclusory allegations that the alternatives would not have caused more harm than good. … *Fifth Third* does not permit the non-specific allegations of this Complaint to withstand a motion to dismiss"); *Jander v. IBM Corp.* (S.D.N.Y. Sept. 7, 2016) ("Because the Amended Complaint offers only a rote recitation of proposed remedies without the necessary facts and allegations supporting [Plaintiffs'] proposition … it fails to meet [*Dudenhoeffer's*] threshold.").

In other cases, courts have gone a step further and found that a prudent fiduciary very well may have concluded that freezing stock purchases and sales would do more harm than good, by signaling to the public that plan fiduciaries viewed the employer stock as a bad investment and causing a greater drop in the stock price than would have been caused by a "wait and see" approach. See *In re Idearc ERISA Litig.* (N.D. Tex. Oct. 4, 2016) ("In *Dudenhoeffer*, the Court noted that the market might take [a plan's freeze of stock purchases] as a sign that insider fiduciaries viewed the employer's stock as a bad investment … causing a drop in the stock price and a concomitant drop in the value of the stock already held by the fund. . . . [Plaintiff] does not elaborate as to how a prudent fiduciary might have perceived such a risk in this case."); *Whitley*, 838 F.3d at 529 ("[I]t does not seem reasonable to say that a prudent fiduciary at that time could not have concluded that … freezing trades of BP stock … which could likely lower the stock price—would do more harm than good. In fact, it seems that a prudent fiduciary could very easily conclude that such action would do more harm than good"); *Martone* (same).

Earlier Disclosure of Inside Information

Another common assertion by the plaintiffs' bar is that the plan fiduciaries should have made public disclosures about the inside information they allegedly possessed because: (i) that would have permitted the market to cause the price of company stock to return to its true value; and (ii) the longer a fraud goes on, the more painful the stock price correction would be. In many cases, these assertions have been rejected upon a finding that the allegations were conclusory. See, e.g., *In re JPMorgan Chase & Co. ERISA Litig.* (S.D.N.Y. Jan. 8, 2016) ("These assertions are not particular to the facts of this case and could be made by plaintiffs in any case asserting a breach of ERISA's duty of prudence."), *aff'd, Loeza v. Does,* 659 F. App'x 44 (2d Cir. 2016); *Jander* (same); *Whitley*, 838 F.3d at 529; *Martone; Wilson.* In other cases, courts have rejected this proposed course of action upon a finding that a prudent fiduciary could have concluded that earlier public disclosure would cause more harm than good. For example, claims that defendants should have made public disclosures during the pendency of an internal investigation have been rejected for failure to allege facts that would have prevented a reasonable fiduciary from concluding that a pre-investigation disclosure would "spark market fears that thorough investigation [would] later show to be unfounded." *In re HP ERISA Litig.* (N.D. Cal. June 15, 2015).

The risk of a market overreaction to public disclosure and the attendant drop in stock price similarly have caused courts to reject allegations that "the longer the fraud goes on, the more painful the correction will be." See *In re JPMorgan Chase & Co. ERISA Litig.;* see also *In re Pilgrim's Pride* (E.D. Tex. Aug. 19, 2016) ("Publicizing all of the negative insider information alleged by Plaintiffs would guarantee the collapse of the company stock … Innumerable things could have happened to avoid the collapse, and it is simply implausible to say that a reasonable fiduciary could not have concluded that accelerating a stock collapse would cause more harm than good."), *adopted*, Oct. 4, 2016; *Martone* ("[I]n light of the negative impact that [public disclosure] would have—a lower stock price—a prudent fiduciary could very easily conclude that such action would do more harm than good").

Seeking Guidance from the SEC or DOL

Some plaintiffs have asserted that plan fiduciaries with knowledge of inside information should have sought guidance from the DOL and/or SEC. In these cases, plaintiffs contend that DOL or SEC would have advised the fiduciaries to resign, and the plan could have retained outside experts as advisors or independent fiduciaries. Here, too, courts have found the pleading of this alternative to be insufficient to satisfy the second prong of *Dudenhoeffer*'s test because plaintiffs had failed to allege how consulting with DOL or SEC would avoid the harm complained of. Even if defendants were to resign, and the plan were to retain outside experts, the courts reasoned, plaintiffs had not established why the new fiduciaries, with knowledge of public information only, would take an alternative course of action such as freezing purchases and sales of employer stock or making public disclosure. See *In re Idearc*; *In re Pilgrim's Pride*.

Proskauer's View

The requirement that a complaint contain facts supporting the proposition that "a prudent fiduciary in the same position could not have concluded that the alternative action would do more harm than good" has proven to be difficult to satisfy. Courts have described this standard as "significant" and "demanding." Indeed, one wonders whether the standard is insurmountable. To date, no court has provided a roadmap as to what type of allegations will suffice to satisfy it. Whether the courts' more rigid position will deter the plaintiffs' bar from pursuing employer stock litigations remains to be seen: the number of new filings has declined dramatically, but this simply may be due to the recent surge in market prices. But whether or not the plaintiffs' bar abandons these claims, the prospects for plaintiffs to proceed with these claims past the pleadings stage seem much bleaker than some had anticipated after *Dudenhoeffer*.

Highlights from the Employee Benefits & Executive Compensation Blog

Health Care Reform

Health Care Reform Update – American Health Care Act Shelved

By Damian A. Myers

The American Health Care Act ("AHCA"), the legislation intended to "repeal and replace" the Affordable Care Act ("ACA"), was shelved on Friday, March 24, 2017, ending for now efforts to repeal the ACA. The AHCA, described in our recent blog entry, was introduced on March 6, 2017 and immediately faced strong opposition from both sides of aisle. After failing to negotiate a compromise, President Trump issued an ultimatum to Congress to pass the legislation by March 24, 2017 or else the ACA would remain in place. Unable to muster enough support for the AHCA, Congress withdrew the bill.

We now enter a new period of uncertainty with respect to the future of health care reform. Consistent with President Trump's ACA executive order issued on his first day in office, his administration could take regulatory and sub-regulatory steps to weaken various ACA requirements as they have developed over the years. It is also possible that, in somewhat of a reversal of course in light of the failure of the AHCA, his administration would leave ACA unchanged under the belief that it is not sustainable and will eventually fail on its own.

Similarly, though some Republican members may continue to push for repeal and replacement, others may be content to leave ACA unchanged in the belief that it will fail on its own. Still others in Congress, potentially on a bipartisan basis, may look to other possible changes in health care law that do not go to the heart of the ACA structure in the same way as the AHCA would have. For example, stand-alone legislation related to health savings account expansion is currently pending. Legislation that would repeal the so-called Cadillac Tax has also been introduced. Bills that would repeal other ACA-related taxes and that would modify rules related to wellness programs have also been drafted. Whether any of these bills will make it to a vote is uncertain.

Despite this uncertainty, employers and plan administrators should continue to comply with the ACA's mandates, including the employer shared responsibility mandate and ACA reporting. Importantly, instead of being delayed until 2025, as would have been the case under the AHCA, the Cadillac Tax is scheduled to become effective beginning in 2020. Though this is more than two years away, employers should begin planning now to minimize the impact of the tax.

American Health Care Act – Key Takeaways for Employers and Plan Sponsors

By Damian A. Myers

On March 6, 2017, the House of Representatives' Ways and Means Committee and Energy and Commerce Committee released budget reconciliation recommendations that will, after mark-up beginning on March 8th, form the American Health Care Act (the "AHCA"). The AHCA is intended to be the law that "repeals and replaces" the Affordable Care Act ("ACA"). The Ways and Means Committee bill certainly repeals most of the taxes applied under the ACA and the Energy and Commerce Committee bill significantly alters Medicaid and how that program is funded. Nevertheless, the AHCA would retain a number of key ACA provisions, albeit modified in some respects.

The proposed AHCA has already faced strong opposition from members of both parties and, thus, it is likely that this legislation will either undergo revisions or be substituted with another bill. In any event, the draft AHCA, when read in conjunction with other recent attempts to repeal and replace the ACA, provides a roadmap of where Congress appears to be heading. Below are key takeaways that employers and plan sponsors should be aware of and a few things they should keep an eye on as things develop.

1. Individual and Employer Mandates

Like other efforts to repeal and replace the ACA, the AHCA would essentially repeal the ACA's individual and employer mandates effective after December 31, 2015. The AHCA does this by "zeroing-out" the penalties for not having minimum essential coverage (individual mandate) or for not offering adequate minimum essential coverage to full-time employees (employer mandate).

Instead of imposing a tax penalty on individuals who do not enroll in minimum essential coverage, the AHCA attempts to encourage individuals to have coverage by allowing insurance carriers to charge a 30% premium surcharge to those who fail to have continuous coverage (i.e., a break in coverage of 63 days or more would trigger the surcharge). Although the AHCA keeps in place the ACA's prohibition against preexisting condition exclusions, the 30% surcharge appears to be another means of discouraging people from waiting until they have a health issue to purchase coverage.

Outside of the effective repeal of the employer mandate, the AHCA's impact on group health plans appears to be minimal. However, if the 30% surcharge is part of the final legislation, it is likely that plan sponsors will be required to provide notices similar to the certificates of creditable coverage required in pre-ACA days.

2. Employer Reporting Obligations to Continue

Although the individual and employer mandates would be repealed, it is likely that the ACA reporting obligations (Forms 1094-B/C and 1095-B/C) will remain in place, at least in some forms. Until 2020, individuals will still be able to get premium credits when purchasing coverage on Marketplaces. Thus, the reporting requirement under Section 6055 of the Internal Revenue Code (the "Code") remains important. With the employer mandate repeal, reporting under Code Section 6056 seems less important, but it may nevertheless continue until 2020. After 2020, tax credits would be available under the AHCA, so the IRS would likely still need employers to report at least some information regarding coverage.

3. Cadillac Tax Repealed (but really just delayed)

Despite the AHCA provision "repealing" the so-called Cadillac Tax, the legislation merely delays the effective date of the tax until 2025. The Cadillac Tax was originally slated to be effective in 2018, but it was delayed until 2020 in prior budget legislation. Given that the AHCA is also budget reconciliation legislation, the newest delay may simply be a procedural step toward future repeal. Employers and plan sponsors should nevertheless keep the Cadillac Tax on their radars.

4. Many ACA-Related Taxes Repealed

The AHCA would repeal or modify, effective after December 31, 2017, numerous taxes created or modified by the ACA, some of which would have a direct or indirect impact on group health plans. For example, the branded prescription drug tax, medical device tax, and the health insurance tax would be repealed. The Medicare tax on investment income and the Medicare surcharge on high-earners would also be repealed. The annual contribution limitation on health flexible spending accounts ("HFSAs") would be removed. The penalty for ineligible distributions (those made before age 65 for non-medical expenses) under health savings accounts ("HSAs") would be reduced to 10%. The Retiree Drug Subsidy would again be deductible.

5. Popular ACA Reforms Remain

Because the AHCA is budget reconciliation legislation, only revenue-related portions of the ACA can be repealed or modified. Thus, various ACA market reforms and patient protections would remain in place. These include:

- The requirement to cover dependent children through age 25;
- The prohibition on waiting periods in excess of 90 days;
- The requirement to cover essential health benefits (individual and small group market plans only);

- The prohibition against lifetime or annual dollar limits on essential health benefits;
- The annual cap on out-of-pocket expenditures on essential health benefits;
- Uniform coverage of emergency room services for in-network and out-of-network visits;
- Required first-dollar coverage of preventive health services;
- The prohibition of preexisting condition exclusions;
- Enhanced claims and appeals provisions; and
- Provider nondiscrimination.

6. Employee Tax Exclusion Remains Intact

Previous attempts to repeal and replace the ACA included revenue-generating provisions to pay for the repeal of the ACA-related taxes. In prior legislation, this would have been accomplished by eliminating or reducing the employer deduction for health benefit expenses or by capping the employee tax exclusion for the cost of coverage. The AHCA does not currently include a similar provision, but it is certainly possible that such a provision can be added as the AHCA is negotiated and revised.

7. HFSA/HSA Expansion

The AHCA also modifies the tax rules related to HFSAs and HSAs. As noted above, the AHCA would remove the annual contribution cap on HFSAs. Additionally, HFSAs and HSAs would now be able to reimburse on a non-taxable basis over-the-counter medication without a prescription. The annual contribution limit to HSAs would be increased to $6,550 (individual) and $13,100 (family). Spouses would both be able to make catch-up contributions to the same HSA.

8. New Tax Credit Scheme Could Cause Administrative Issues for Plan Sponsors

What appears to be one of the more politically controversial aspects of the AHCA is the new advanced tax credit scheme. At its core, the AHCA proposal is very similar to the premium tax credits available under the ACA – individuals would get an advanced tax credit to help pay for individual insurance market premiums. The amount of the credit would be based on age and would be available only to individuals with income less than $75,000 (individual) or $150,000 (jointly with a spouse). The credit would be administered under the rules similar to the Health Coverage Tax Credit (“HCTC”) (see our July 16, 2015 blog entry for more information on the HCTC).

Individuals enrolled in group health plans would not eligible for the tax credit, unless they are enrolled in COBRA coverage that is not subsidized by the employer. Importantly, in order to receive the credit, the coverage (whether individual market or COBRA) cannot cover services related to abortion (subject to certain exceptions).

This arrangement would likely create administrative headaches for plan sponsors and COBRA administrators. The new tax credit scheme appears to require monthly reporting by eligible coverage providers, so COBRA administrators would have to develop procedures to comply with this requirement. Employers sponsoring plans that cover abortion services will need to consider the impact that will have on COBRA qualified beneficiaries. Providing COBRA coverage that covers abortion will prevent a qualified beneficiary from getting a tax credit, but simply carving abortion coverage out from COBRA coverage is not likely a viable option because COBRA coverage must be identical to active employee coverage. Should this provision find its way to the final legislation, plan sponsors and COBRA administrators will need to work with counsel and other consultants to develop a compliance strategy.

Given the opposition the AHCA is facing, it is very likely that there will be changes to the legislation as it makes its way through Congress. We will continue to monitor legislative efforts and will provide updates as substantive developments occur.

Notice Requirement for Small Employer HRAs Delayed Pending Regulations

By Damian A. Myers

On February 27, 2017, the Internal Revenue Service issued Notice 2017-20 delaying the notice requirement for qualified small employer health reimbursement arrangements (“QSEHRAs”). By way of background, prior to enactment of the 21st Century Cures Act (“Cures Act”) in December 2016, the Affordable Care Act prohibited HRAs unless they were integrated with group health plans. This meant that HRAs could not be used to reimburse premiums purchased on the individual market. The Cures Act created QSEHRAs so that small employers could offer non-integrated HRAs that would enable employees to, among other things, purchase individual market coverage. Additional detail on QSEHRAs and their requirements can be found in our December 19, 2016 blog entry.

One of the requirements for QSEHRAs is that employees must receive a written notice no later than 90 days before the start of the plan year (or the start of eligibility for a new employee) describing the amount of reimbursement available under the QSEHRA and explaining that the employee must disclose the presence of the QSEHRA when applying for or renewing coverage purchased from the Marketplace. If an employer fails to provide the notice, the employer could face a penalty of $50 per employee per failure with a maximum penalty of $2,500.

Under the Cures Act, QSEHRAs in place on January 1, 2017 were required to provide this notice no later than March 13, 2017 (i.e., 90 days after enactment of the Cures Act). However, the IRS has not yet published regulations or other guidance governing the operation of these arrangements. In the absence of guidance, the IRS issued Notice 2017-20 to delay the notice requirement and suspend potential notice penalties until the IRS issues further guidance. Once guidance is issued, employers will have at least 90 days to provide the QSEHRA notice to employees.

Mental Health Parity Act

Class Certified in Claims for Autism Treatment Coverage

By Steven A. Sutro

A federal district court in the Western District of Kentucky certified a class of participants and beneficiaries in plans sponsored by Anthem Health Plans of Kentucky, Inc. who had been denied coverage or reimbursement for Applied Behavior Analysis (ABA) for Autism Spectrum Disorder (ASD). Plaintiff claimed that the time and dollar limitations violated ERISA and the Mental Health Parity and Addiction Equity Act. In so ruling, the court found that plaintiff satisfied the requirements of Rule 23, and rejected Anthem's argument that individualized issues related to each class member's condition and treatment made a class action an improper method for resolving the dispute. The case is *Wilson v. Anthem Health Plans of Kentucky, Inc.*, No. 3:14-CV-743-TBR, 2017 WL 56064 (W.D. Ky. Jan. 4, 2017).

Retiree Benefits

Fourth Circuit Rejects Retirees' Claim for Vested Health Benefits

By Madeline Chimento Rea

The Fourth Circuit upheld an employer's unilateral decision to amend a collective bargaining agreement to cap employer contributions to retiree health benefits and freeze Medicare reimbursements for hourly retirees. In so ruling, the Court applied general contract principles, as required by the Supreme Court's decision in *M&G Polymers USA, LLC v. Tackett*, 135 S. Ct. 926 (2015), and concluded that: (i) the applicable CBA and SPD were properly construed to limit the provision of retiree health benefits to the term of the agreement, which meant that the benefits did not vest; and (ii) because the SPD unequivocally stated that pension benefits vested, it was reasonable to conclude that the parties did not intend for health benefits to vest. The case is *Barton v. Constellium Rolled Prods.-Ravenswood, LLC*, No. 16-1103, 2017 WL 1078540 (4th Cir. 2017).

Conflict of Interest Rule

No Emergency Injunction Appeal in Chamber's Challenge to DOL Rule

By Russell Hirschhorn and Benjamin Saper

On March 20, 2017, a federal court in the Northern District of Texas denied the U.S. Chamber of Commerce's emergency motion for an injunction pending appeal challenging implementation of the Department's conflict of interest rule and related exemptions. The court applied the standard for evaluating a preliminary injunction motion and concluded that: (i) the Department already had prevailed on summary judgment (see our blog available here); (ii) the potential for irreparable harm to Plaintiffs was small because the Department had proposed a delay in the rule's applicability date; (iii) the Department would be harmed by an injunction because it "would interfere with the Department's statutory authority, its expertise, and its policy-making role;" and (iv) the public interest weighed against granting an injunction because the Department had already made reasonable conclusions during the rule making process that the rule was in the public interest. The case is *Chamber of Commerce v. Hugler, No. 3:16-cv-01476-M, 2017 BL 87076 (N.D. Tex. Mar. 20, 2017).*

IRS Issues Temporary Enforcement Policy In Line with DOL FAB 2017-01

By Russell Hirschhorn and Benjamin Saper

On the heels of the Department of Labor's temporary enforcement policy concerning the DOL conflict of interest rule and related exemptions (see our blog post here), the IRS announced that it is providing relief from excise taxes under Code § 4975 that conforms to the DOL's temporary enforcement policy described in FAB 2017-01. The IRS's action ensures that enforcement of the prohibited transaction rules by DOL and IRS will remain in synch.

U.S. DOL Proposes Delay of Conflict of Interest Rule and Related Exemptions

By Russell Hirschhorn, Seth Safra and Benjamin Saper

On March 1, 2017, the U.S. Department of Labor proposed a 60-day delay of the conflict of interest rule and related exemptions (currently set to be applicable on April 10, 2017). The Department opened two comment periods related to the rule:

1. A 15-day comment period (ending March 17, 2017) on whether enforcement of the rule should be delayed; and
2. A 45-day comment period (ending April 17, 2017) on the rule's substance.

The proposal and requests for comments relate to President Trump's Memorandum, issued on February 3, 2017, in which he directed the Department to examine the rule and related exemptions and prepare an updated economic and legal analysis concerning their likely impact, including:

- Whether the anticipated applicability of the final rule has harmed or is likely to harm investors due to a reduction of Americans' access to certain retirement savings offerings, retirement product structures, retirement savings information, or related financial advice;
- Whether the anticipated applicability of the final rule has resulted in dislocations or disruptions within the retirement services industry that may adversely affect investors or retirees; and
- Whether the rule is likely to cause an increase in litigation, and an increase in the prices that investors and retirees must pay to gain access to retirement services.

The President directed that if the Department concludes for any reason that the rule and related exemptions are inconsistent with the Administration's priority "to empower Americans to make their own financial decisions, to facilitate their ability to save for retirement and build the individual wealth necessary to afford typical lifetime expenses, such as buying a home and paying for college, and to withstand unexpected financial emergencies," then the Department must propose to rescind or revise the rule.

The proposed 60-day delay observes that the time required for the review directed by the February 3 Memorandum will extend past the rule's April 10 scheduled applicability date. Furthermore, the Department noted the potential for disruption and unnecessary compliance expenditures if the rule is allowed to go into effect when there is still a chance of rescission or significant revisions. The proposal also notes that a 60-day delay might not be sufficient for the Department to complete its work and requested comments on the impact of a longer delay – "6 months, a year, or more".

View From Proskauer – While no one can predict the future, the proposed rule suggests that the Department is taking a close look at the rule and related exemptions and is prepared to delay the rule's applicability date until it is comfortable that the rule strikes an appropriate balance between regulatory burdens and protecting against conflicts of interest. Although the administration has made public statements denigrating the rule, the proposal suggests that full rescission is not a fait accompli. We expect to hear comments from diverse interests over the next 15 days, arguing for and against a delay of the applicability date. It also is reasonable to expect that the Department will wait to make final decision until after a Secretary of Labor is confirmed and leadership of the Employee Benefits Security Administration is in place, to allow the new leadership sufficient time to review the rule and its impact before starting to enforce it or proposing major changes (or full rescission).

USDOL Prevails in Kansas in Another Decision on Fiduciary Rule

By Russell Hirschhorn and Benjamin Saper

On February 17, 2017, a federal district Court in Kansas upheld the U.S. Department of Labor's conflict of interest rule and related exemptions in a suit brought by Market Synergy Group, Inc. This ruling on the merits follows the court's prior ruling in November 2016 denying Market Synergy Group's request for a temporary injunction. The court determined that: (1) the Department satisfied the Administrative Procedure Act's requirement of providing fair notice of the proposed rule change; (2) the Department's decision to treat fixed indexed annuities differently than all other fixed annuities in PTE 84-24 was not arbitrary and capricious; (3) the Department adequately considered the economic impact that the final rule would impose on independent insurance agent distribution channels; and (4) the Department's issuance of PTE 84-24 does not exceed the agency's statutory authority. The case is *Mkt. Synergy Grp., Inc. v. United States Dep't of Labor, No. 16-CV-4083-DDC-KGS, 2016 WL 6948061 (D. Kan. Nov. 28, 2016).*

Like the prior rulings, the court's decision relates only to the Department's authority to issue the rule. It does not address the Trump administration's proposal to delay or change the rule. A delay proposal is currently being reviewed by the Office of Management and Budget, and is expected to be released in the next couple weeks.

Update on the USDOL Conflict of Interest Rule and Related Exemptions

By Russell Hirschhorn and Benjamin Saper

There were two key developments last week concerning the ongoing challenges to the U.S. Department of Labor (USDOL) conflict of interest rule and related exemptions: a Presidential Memorandum calling for a review of the rule, and a ruling by a federal court in Texas rejecting the U.S. Chamber of Commerce's challenges to the rule.

Presidential Memorandum

On February 3, 2017, President Trump issued a Presidential Memorandum ordering the USDOL to conduct an economic and legal analysis of the conflict of interest rule and associated exemptions. The Memorandum requires the USDOL to rescind the rule if it finds that it is inconsistent with the Trump Administration's policies. The Memorandum does not explicitly call for an extension of the rule's April 10, 2017 applicability date. However, the USDOL has filed a notice with the Office of Management and Budget indicating that it intends to delay implementation and open up a new comment period. The details have not been made public.

District Court Decision

On February 8, 2017, a federal district court in Texas granted the USDOL's motion for summary judgment and rejected the

Chamber of Commerce's many challenges to the conflict of interest rule and related exemptions. This decision represents the third federal district court to uphold the rule and exemptions as a permitted exercise of the USDOL's authority. It followed federal district courts in Washington D.C. and Kansas. The decision does not opine on the new administration's authority to rescind the rule, delay enforcement, or issue a different rule, subject to the procedural requirements of the Administrative Procedure Act.

Exhaustion

Sixth Circuit: ERISA Exhaustion Not Required in Plan Amendment Suit

By Steven A. Sutro

The Sixth Circuit held that retirement plan participants were not required to exhaust their administrative remedies prior to bringing a claim alleging that a plan amendment violated ERISA. In so holding, the Court agreed with the opinions of the Third, Fourth, Fifth, Ninth, Tenth, and D.C. Circuits and disagreed with the opinions of the Seventh and Eleventh Circuits. In the view of the Sixth Circuit, challenges that are "directed to the legality of the plan, not to a mere interpretation of it," do not require exhaustion. The case is *Hitchcock v. Cumberland Univ. 403(b) DC Plan, No. 16-5942, 2017 WL 971790 (6th Cir. Mar. 14, 2017).*

403(b) Plans

IRS Announces the Last Day of the Remedial Amendment Period for 403(b) Plans

By Steven Einhorn

The Internal Revenue Service recently issued Revenue Procedure 2017-18, which provides that the last day of the remedial amendment period for Code Section 403(b) retirement plans will be March 31, 2020. As discussed below, this means that a sponsor of a Code Section 403(b) plan who timely adopted a Code Section 403(b) retirement plan document that was intended to comply with the Code will have until March 31, 2020 to retroactively correct any defects to the form of the plan document, either by amending its plan document or adopting a pre-approved plan document.

Background

Under final Treasury regulations that were issued in 2007, effective January 1, 2009, a sponsor of Code Section 403(b) retirement plan is generally required to maintain its plan pursuant to a written plan document that complies with the requirements of these final Treasury regulations in both form and operation.

In March of 2013, the IRS issued Revenue Procedure 2013-22, which set out new procedures for the IRS to issue opinion and advisory letters for pre-approved plan documents for Code Section 403(b) retirement plans (*i.e.*, prototype and volume submitter plan documents). The IRS does not issue determination letters on individually designed Code Section 403(b) retirement plans.

Revenue Procedure 2013-22 also included information about a remedial amendment period that would allow a plan sponsor to retroactively correct defects in the form of its Code Section 403(b) plan document, provided that the correction is made prior to the end of the remedial amendment period. For this purpose, a "defect" is a provision, or absence of a required provision, that causes the plan to fail to satisfy the requirements of Code Section 403(b). Generally, the remedial amendment period is available only if an employer adopted a written plan document intended to satisfy the requirements of Code Section 403(b) on or before January 1, 2010 or, if later, the first day of the plan's effective date. Revenue Procedure 2013-22 provided that any defect must be corrected on or before the last day of the remedial amendment period. However, the guidance did not state when the last day of the remedial amendment period would occur.

The Last Day of the Remedial Amendment Period Announced

With the issuance of Revenue Procedure 2017-18, the IRS announced that the last day of the remedial amendment period for Code Section 403(b) retirement plans will be March 31, 2020. Therefore, if the form of a Code Section 403(b) retirement plan does not satisfy the requirements of Code Section 403(b) during the remedial amendment period but is properly retroactively amended by March 31, 2020, the plan will be considered to have satisfied the requirements for the entire remedial amendment period (which begins on January 1, 2010 or, if later, the effective date of the plan). Generally, a Code Section 403(b) retirement plan will automatically satisfy the IRS requirements that the form of the document complies with the Code Section 403(b) if the plan sponsor adopts a pre-approved plan document on or before the last day of the remedial amendment period.

According to Revenue Procedure 2017-18, the Department of Treasury and IRS intend to issue future guidance with respect to the timing of Code Sec. 403(b) retirement plan amendments made after Mar. 31, 2020.

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