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ENERGY LAW REPORT

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Now. Normal. Next.
Benefits and Compensation Challenges in a Return to Work Environment

*By Althea R. Day, R. Randall Tracht, and Jonathan Zimmerman**

The authors discuss how federal stimulus legislation may affect a variety of decisions by energy companies implicating the employer-employee relationship.

As energy companies, along with a host of other businesses, gradually return to ostensibly "normal" operations following the disruptions brought on by the COVID-19 pandemic, such employers may nevertheless confront a drastically altered business environment. Many may be considering difficult decisions to cope with the economic fallout of the health crisis, including reductions in personnel or compensation.

On the plus side, federal stimulus legislation, such as the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act"), may affect a variety of decisions implicating the employer-employee relationship, as well as determinations on payroll taxes, retirement plans, and health and welfare benefit issues.

WORKFORCE CHANGE AND SEVERANCE PLANS

Employers considering either voluntary or involuntary workforce reductions—or some combination of the two—as an initial step may want to consider reviewing and updating their existing severance plans and policies. This column could entail a few simple updates all the way up to a comprehensive overhaul of the severance plan to reflect the company's individual situation.

A threshold issue to consider is the extent to which an employer's severance plan is subject to the Employee Retirement Income Security Act ("ERISA"). Some employers may not treat their severance programs as being subject to ERISA and, instead, view them as simple payroll practices. By contrast, other employers treat their severance programs as formal plans that are subject to ERISA. Which approach is correct?

The answer depends on the facts and circumstances and whether there is an "administrative scheme" that supports the existence of an employee benefit plan for purposes of ERISA. In evaluating these issues, courts have found that where there is an ongoing program of providing benefits that requires administration

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and discretion (e.g., eligibility determinations, calculations to determine benefits, the payment of benefits over time, etc.), there likely is an administrative scheme supporting the existence of a plan for purposes of ERISA. By contrast, a program that pays a one-time severance payment to all employees in the same amount and without distinction as to eligibility may not be a plan for purposes of ERISA.

Employers that are not mindful of these considerations may accidentally create an ERISA severance plan by having an administrative scheme and a regular policy of paying severance. And without the benefit of a formal ERISA plan document and consideration of ERISA's reporting and disclosure requirements, employers may inadvertently fail to satisfy certain compliance obligations.

In addition, employers may find that embracing ERISA plan status is desirable for a number of reasons, including the application of federal law to disputes arising under an ERISA-covered plan, which may allow employers to avoid claims under certain state specific laws. Also, under an ERISA-covered plan, employers can retain discretion as to eligibility and benefit determinations and retain the right to amend or terminate the plan at any time and for any reason.

By contrast, companies relying on informal arrangements or non-ERISA plans may find themselves subject to a court's determination regarding the de facto existence of a contractual severance benefit, potentially exposing the company to unexpected severance obligations.

An ERISA plan also conveys the benefits of certain procedural rules. ERISA plans provide for an established administrative process for handling claims and appeals and courts generally have been willing to enforce other plan-based features, such as reasonable statutes of limitations for bringing claims and choice of venue provisions.

FRINGE BENEFIT AND PAYROLL TAX ISSUES

The CARES Act contains two employment tax provisions offering relief to employers, including the ability to defer payroll taxes and a credit for employee retention.

Under the first provision, employers, regardless of the size of their workforces, can delay paying the employer's share of Social Security taxes due between March 27, 2020, and January 1, 2021. Essentially, this amounts to an interest-free loan from the government with repayment not required until much later (half the deferred taxes are due by December 31, 2021, and the other half are due by December 2022). Employers can utilize this deferral in addition to the employee retention credit explained below, and the loan forgiveness provisions in the CARES Act's Paycheck Protection Program do not affect eligibility.

Unfortunately, there currently is no way to recover Social Security taxes paid on or after March 27 and before the employer started deferring these taxes. This means that employers can defer payments only on a prospective basis. While the American Bar Association and others have pushed back on this, so far the government has not provided relief.

The employee retention credit allows for up to $5,000 in refundable tax credits for qualified wages paid to employees by an eligible employer. This complicated provision requires, first, that an employer must figure out if it qualifies, then determine which wages qualify, and finally decide how to claim the benefit.

An employer qualifies for the credit if the employer's business is fully or partially shut down because of a COVID-19-related government order, or if the employer suffers at least a 50 percent decline in quarterly gross receipts compared to the corresponding quarter in 2019. It can be difficult for an essential business to meet the shutdown test, but it is not impossible, particularly if a portion of the business was shut down or subject to certain other restrictions on business operations. The determination will vary based on the employer's individual facts and circumstances.

For employers that averaged more than 100 full-time employees in 2019, qualified wages are wages paid to employees who are not working because of the same circumstances that caused the employer to qualify for the credit. For employers that averaged 100 or fewer full-time employees in 2019, wages paid to all employees may qualify. Employer payments for health insurance premiums also may qualify for the credit. The credit is 50 percent of qualified wages, up to a maximum credit of $5,000 per employee.

The credit can be claimed by simply not paying employment taxes due to the Internal Revenue Service ("IRS"). For example, if an employer calculates it has $20,000 of qualified wages—meaning it is eligible for a $10,000 credit—the employer can simply hold back $10,000 from the employment taxes the employer otherwise would pay to the IRS.

The employer also can claim the credit in advance by filing Form 7200 with the IRS, or in arrears on the employer's quarterly tax return. An employer that initially does not claim the credit may apply for a refund by filing a corrected employment tax return. A refund claim may be the safest approach for employers who are unsure whether they qualify for the credit.

RETIREMENT PLAN ISSUES

The CARES Act provides 401(k) plan participants enhanced access to their retirement savings and delays the impact of certain otherwise adverse consequences, although it leaves the adoption of these new provisions up to the

employer. These provisions ease certain restrictions or penalties on employees taking distributions from or loans against their retirement plans, and increases allowable loan amounts. Qualifying employees are those that self-certify as to having been negatively impacted by COVID-19 or having a spouse or other household member negatively impacted.

Some employers also may be considering the difficult decision to suspend employer contributions to their 401(k) or other defined contribution plans. In many instances, employers can suspend ongoing and periodic contributions with nothing more than a plan amendment.

However, in cases such as those involving "safe harbor" 401(k) plans, advance notice to employees is required and the employer loses its automatic pass for certain non-discrimination tests for the year, along with other complications.

The CARES Act additionally provided relief for employers offering defined benefit plans, primarily addressing contribution timing requirements intended to assist the employer's 2020 cash flow. For instance, the CARES Act allows pension plan sponsors to delay making minimum required contributions due in the 2020 calendar year, however these contributions are required to be made, with interest, in 2021. As we write this, there remain many unanswered questions with respect to this relief, including how this affects non-calendar-year plans and the deductibility of delayed contributions, among other issues.

EXECUTIVE COMPENSATION

Many companies now grapple with the question of how to retain their key executives while aligning their compensation with the organization's current economic realities. They may consider a number of options, including a temporary salary reduction, deferring a portion of executives' salaries to a later tax year, or exchanging a portion of base salary for company stock. Each of these options raises its own set of considerations.

For instance, companies considering a reduction in base salary need to examine the executive's employment agreement to understand whether that compensation change may allow the executive to resign and claim severance benefits. The company's equity plan documents may also come into play regarding swapping salary for stocks.

Further, companies should know that the IRS likely intends to take a hard look at any mid-year changes to compensation rights. Another area of risk: conflicts with existing employment agreements could trigger breach of contract claims.

Some corporations may decide to delay significant changes based on their assessment of how long the pandemic conditions will last. Other likely

considerations for employers include the impact any changes might have on employee retention and future recruitment; how any changes might be viewed in the context of a corporate change in control; the tax implications for employees; and possible effects of changes on performance goals.

HEALTH AND WELFARE PLANS EXTENDED DEADLINES AND CLAIMS PERIODS

For health and welfare plans, legislation and agency guidance provide additional flexibility in 2020 for employees to make mid-year election changes. These include extending deadlines to participate in COBRA, permitting mid-year election changes for employer-sponsored health coverage, and more. While employers do not need to offer all these election changes, good faith requirements remain in place, including prompt communication to employees.

CONCLUSION

As energy companies return to the new “normal” in operations, there is much to consider related to workforce changes including separating employees, reducing compensation, and mandates and optional relief with respect to payroll taxes and employer-provided benefits. Each of these areas potentially raise a multitude of complex issues that require careful consideration.