ERISA ROUNDUP

A quarterly recap of recent publications from BDO's ERISA Center of Excellence.

Q1 2021

A NOTE FROM BDO'S NATIONAL ERISA PRACTICE LEADER

As everyone shakes off the winter cold and prepares for spring, BDO's ERISA Center of Excellence has been working diligently to bring you a fresh set of insights around the latest topics in employee benefit plans.

We are excited to announce a brand-new avenue where you can hear about all things ERISA and other HR-related topics in our recently launched podcast series, BDO Talks ERISA! In keeping with the theme of the upcoming National Employee Benefits Day (April 6), our latest episode focuses on mental wellness and tips to avoid burnout. This Roundup includes all of the details on current podcast episodes. Be sure to join our conversation at **BDO Talks ERISA** and connect to let us know what you like (and what topics you would like to hear more about in future episodes!).

In addition to insights to help you navigate the CARES Act and other regulatory relief efforts, SAS 136, and much more, we close out this quarter reflecting on the disproportionate strain the pandemic has placed on the financial wellness of women. We share practical tips for employers seeking to initiate better financial preparedness among their female employees.

As always, I encourage you to follow along with our regular insights at www.bdo.com/erisa.

Sincerely,

BETH GARNER
National Practice Leader, ERISA

BDO's ERISA Center of Excellence is your source for insights on emerging regulations, industry trends, current topics, and more. Visit us at www.bdo.com/erisa or follow along on Twitter: @BDO_USA and #BDOERISA.

IN THIS ISSUE

www.bdo.com/erisa

2021 Deadlines and Important Dates for Plan Sponsors

Sponsors of defined benefit and defined contribution plans should keep the following deadlines and other important dates in mind as they work toward ensuring compliance for their plans in 2021. Dates assume a calendar year plan.

APRIL

- **1** / Action: Hire auditor (if needed) by April 1.
- **1** / RMD: April 1 Deadline for 5 percent business owners and terminated participants who turned 70 ½ in 2020 to receive their required minimum distribution (RMD). Participants who turn 72 during 2021 will be required to start by April 1, 2022.
- **15** / Fund: Corporations and sole proprietors that are not getting an extension must fund contributions by April 15 and receive tax deduction for the prior year.
- **15** / April 15, possible first quarter 2021 contribution due for defined benefit pension plans
- **15** / Fund: IRA contributions for the prior tax year must be funded by April 15.
- **15** / Fund: Participants who contributed over 402(g) or 415 limits in the previous year must be refunded the excess amount by April 15.
- **15** / Action: File PBGC Form 4010 by April 15, Notice of Underfunding for single-employer defined benefit plans with more than $15M aggregate underfunding.
- **26** / Action: File PBGC Form 200 by April 26, if plan sponsor of a single-employer defined benefit plan does not make the April 15 required contribution, causing the plan to have more than $1 million in unpaid contributions.
- **28** / Distribution: Send annual funding notice to participants of single- and multi-employer defined benefit plans over 100 participants by April 28.
- **30** / Distribution: Single-employer defined benefit plans that are less than 60 percent funded must inform participants by April 30 or 30 days after the benefit restriction is determined.

MAY

- **14** / File PBGC Form 10, by May 14, if a defined benefit plan with >100 participants 1) missed its April 15 required contribution, 2) the contribution is still unpaid as of May 15, 3) the contribution could not have been met with a Prefunding or Carryover Balance election and 4) a PBGC Form 200 was not already filed for the same event.
- **14** / Distribution: Defined contribution plans must send fee and benefit information to participants by May 14.
- **15** /Action: File PBGC Form 10 by May 15, Post-Event Notice of Reportable Events if plan sponsor of a single-employer defined benefit plan does not make an April 15 required contribution, causing the plan to have more than $1 million in unpaid contributions.

JUNE

- **29** / Action: Plans with publicly traded employer stock that use an ERISA format must file Form 11-K with the Securities and Exchange Commission by June 29.

JULY

- **14** / Action: Plans with publicly traded employer stock that use an ERISA format that requested a 15 calendar day extension (Form 12b-25) for the Form 11-K must file the Form 11-k with the Securities and Exchange Commission by July 14.
- **26** / Action: File PBGC Form 200 by July 26, if plan sponsor of a single-employer defined benefit plan does not make a July 15 required contribution, causing the plan to have more than $1 million in unpaid contributions.
- **15** / July 15, possible second quarter 2021 contribution due for defined benefit pension plans

AUGUST

- **2** / Action: Large plan audit must be completed by Aug. 2 to avoid requesting Form 5500 extension.
- **2** / Action: IRS Form 5500 must be filed by Aug. 2.
- **2** / Action: To request a Form 5500 extension, Form 5558 must be submitted by Aug. 2.
- **2** / Action: Pay Patient-Centered Outcomes Research Institute (PCORI) fee by Aug 2. Self-insured health plans must pay $2.66 per person (covered by health plan).
- **13** / File PBGC Form 10, by Aug 13, if a defined benefit plan with >100 participants 1) missed its July 15 required contribution, 2) the contribution is still unpaid as of Aug 15, 3) the contribution could not have been met with a Prefunding or Carryover Balance election and 4) a PBGC Form 200 was not already filed for the same event.
- **31** / Best Practice: Plans that failed compliance testing may take this mid-year opportunity to run compliance tests. Aug. 31

SEPTEMBER

- **15** / Fund: If an extension was filed, Sept. 15 is the deadline to fund employer contributions.
- **15** / Fund: Minimum funding deadline for single- and multi-employer defined benefit plans.
- **15** / Sept 15, last date to make 2020 contributions for defined benefit pension plans.
- **25** / Action: File PBGC Form 200 by Sept. 25, if plan sponsor of a single-employer defined benefit plan does not make the Sept. 15 required contribution, causing the plan to have more than $1 million in unpaid contributions.
- **30** / Distribution: Sept. 30, Summary Annual Report sent to participants with Dec. 31 plan year end.

OCTOBER

- **1** / Best Practice: Make sure procedures align with language in plan document. Oct 1.
- **1** / Distribution: Annual notices to participants begin Oct. 1, including 401(k) Plan Safe Harbor Notice, automatic contribution arrangement safe harbor and qualified default investment alternative.
- **15** / File PBGC Form 10, by Oct 15, if a defined benefit plan (of any size) 1) missed its Sept 15 required contribution, 2) the contribution is still unpaid as of Oct 15, 3) the contribution could not have been met with a Prefunding or Carryover Balance election and 4) a PBGC Form 200 was not already filed for the same event.
- **15** / Oct 15, possible third quarter 2021 contribution due for defined benefit pension plans
- **15** / Action: Oct. 15 is the extended deadline for filing Form 5500, including Schedule SB (single employer defined benefit plans) or Schedule MB (multiemployer defined benefit plans)
- **15** / Action: Oct. 15 is the extended deadline for filing individual and C-Corp tax returns.
- **15** / Action: Oct. 15, multi-employer defined benefit plans file PBGC Comprehensive Premium document and pay $29 per participant flat-rate premium.
- **15** / Action: Oct. 15 to open a Simplified Employee Pension (SEP) plan for extended tax filers.
- **25** / Action: File PBGC Form 200 by Oct. 25, if plan sponsor of a single-employer defined benefit plan does not make the Oct. 15 required contribution, causing the plan to have more than $1 million in unpaid contributions.
- **30** / Distribution: Single-employer defined benefit plans that are less than 60 percent funded must inform participants by October 30 or 30 days after the benefit restriction is determined.

NOVEMBER

- **15** / File PBGC Form 10, by Nov 15, if a defined benefit plan with >100 participants 1) missed its Oct 15 required contribution, 2) the contribution is still unpaid as of Nov 15, 3) the contribution could not have been met with a Prefunding or Carryover Balance election and 4) a PBGC Form 200 was not already filed for the same event.

DECEMBER 2021

- **1** / Distribution: Annual Participant notices must be distributed by Dec. 1. These include: 401(k) safe harbor, annual automatic contribution and qualified default investment alternative (QDIA) notices. Effective in 2020, plans that provide the Qualified Non-Elective Contribution Safe Harbor and are not subject to automatic enrollment are not required to provide a written annual notice.
- **15** / Action: Dec. 15 is the extended deadline to distribute Summary Annual Report (SAR) for calendar year plans.
- **31** / Action: Dec. 31 is the final deadline to process corrective distributions for failed ADP/ACP testing; a 10 percent excise tax may apply.
- **31** / Action: Amendments to change traditional

In addition to those important deadlines and dates, plan sponsors should be aware of the contribution plan limits and other rolling notices for 2021:

- Employee salary deferral limits for 401(k), 403(b) and 457 plans will be $19,500. Age 50 catch-up contribution limit increases to $6,500.
- Health Savings Account contribution limit is $3,600 (single) and $7,200 (family). Age 55 catch-up contribution stays at $1,000.
- Traditional and Roth Individual Retirement Account contribution limit will be $6,000. catch-up contributions for participants age 50 and over is $1,000.
- Limitation for the annual benefit under a defined benefit plan under Section 415(b)(1)(A) will be $230,000.
- The dollar amount used to define “highly compensated employee” under Section 414(q)(1)(B) will be $130,000.
- Newly eligible employees must receive a Summary Plan Description (SPD) within 90 days after becoming covered by the Plan.
- Provide quarterly statements and fee information to participants.

New Podcast! BDO Talks ERISA

In February, our ERISA Center of Excellence launched a monthly podcast - BDO Talks ERISA! This series covers best practices around all things ERISA and any other HR-related topics, including:

- How to avoid common compliance issues
- How to navigate the ins-and-outs of ERISA's fiduciary provisions
- Our own experiences working for BDO's ERISA Services group
- A deeper dive into the insights we share through our BDO ERISA Center of Excellence

Listen to new episodes at BDO.com/BDOTalksERISA or subscribe on Apple Podcast or Spotify. If you have suggestions for future topics or have a question for us to answer, send an email to BDOTalksERISA@bdo.com.

CURRENT EPISODES

Episode 1: So Let's Talk: Telehealth and Other Employee Benefit Trends for 2021

On our initial episode of BDO Talks ERISA, meet our co-hosts, Beth Garner, Joanne Szupka and Luanne MacNicol. Today we discuss what plan sponsors need to be aware of as the first quarter of the year begins to wind down. We cover what plan sponsors need to do when they are getting ready to re-engage their workforce, the different communications you need to consider based on different generations, cybersecurity risks, and trends emerging in the employee benefit landscape.

LISTEN TO EPISODE 1 NOW

Episode 2: Don't you 'SAS' me! Gut Check on the SAS-136

Erin Breit, Audit Partner at BDO with over 16 years of accounting experience and AICPA employee benefits expert panelist, joins us to share a little bit about the new auditing standard that's coming up and what plan sponsors need to prepare for.

LISTEN TO EPISODE 2 NOW

Episode 3: Hit the Easy Button: Prepare for the Long-Term, Part-Time Employees Provision of SECURE Act

Thinking about waiting until 2024 to worry about calculating hours for your long-term, part-time employees? Think again! On this episode we speak with Norma Sharara, Managing Director with BDO's National Tax Office. She has over 25 years of experience in the compensation and benefits arena and understands retirement plans inside and out. Norma shares what you need to know about the latest updates to the SECURE Act and its long-term, part-time employees in this episode.

LISTEN TO EPISODE 3 NOW

Episode 4: ESG Investments: More Than Window Dressing

Michael Lynch joins us to discuss investing in ESGs. Michael is a Senior Wealth Manager with BDO Wealth Advisors and a member of the BDO Investment Committee. Michael's primary responsibility is to develop customized, comprehensive, and understandable tax-aware solutions that integrate financial planning and investment management. Michael gives us a look behind the curtain at what you need to know about ESGs and fiduciary requirement.

LISTEN TO EPISODE 4 NOW

Episode 5: Feeling the Burn: A Mental Health Expert Weighs in on Employee Burnout

In this episode, we are joined by Licensed Clinical Social Worker Margaret McDaniel. Margaret lends us her expertise on the relationship between employee burnout and mental health and the various stressors impacting the wellbeing of the workforce. What can your company do to create a culture of acceptance?

LISTEN TO EPISODE 5 NOW

Strengthening Women's Financial Wellness in the Wake of the Pandemic

While nearly everyone has been affected by the COVID-19 pandemic, the economic impact has been especially acute for women. In addition to the disproportionate number of women who were furloughed or laid off, many women faced additional financial stress from needing to take time off to care for children, elderly parents, or other family members.

This is more than just an employee-morale issue for employers. Stress about financial issues can have a meaningful impact on worker productivity. A **Retirement Advisor Council** report found that about half of employees who are distracted by their finances spend at least three work hours a week dealing with issues related to their personal finances.

Now that vaccines are being distributed and more people are returning to work, plan sponsors have an opportunity to take a look at financial wellness programs to help their female employees deal with the myriad financial burdens set upon them by the pandemic.

A WIDENING GAP IN FINANCIAL WELLNESS

Even before the pandemic, there was a significant gap in the financial preparedness of women and men. According to a National Institute on Retirement Security **study**, in 2016, women age 65 and older had a median household retirement income of $47,244 compared with $57,144 for men. This gap has many causes, including women being more likely to take time off of work to care for children.

The gap appears to be widening because of the pandemic. According to a March 2021 **report** by the National Women's Law Center (NWLC), more than 2.3 million women left work during the 12 months ending in February 2021 compared with 1.8 million men. One driver of this disparity is that many women work in hospitality, education, healthcare, retail, and other industries that were immensely affected by the pandemic.

Thus, it is not surprising that nearly three-fourths of women reported that the pandemic has had a negative impact on their retirement savings, according to a January 2021 **study** by the Nationwide Retirement Institute. Approximately 40% of female respondents to a December 2020 Transamerica Center for Retirement Studies **survey** said that they weren't confident that they would retire comfortably, compared to 24% of men. Women also reported saving less, dipping more into their retirement accounts and juggling more short-term financial issues than men.

TAILORING FINANCIAL WELLNESS TO WOMEN'S TOP PRIORITIES

Employers can play a leading role in getting female employees back on track with their retirement savings and strengthening their overall financial preparedness. Financial wellness programs can take many forms, but in general they are educational programs designed to help boost employees' confidence and preparedness on issues such as saving for retirement, investing, budgeting, managing debt, taxes, and more.

An important aspect of creating a financial wellness program that empowers women is to tailor the content to the topics that women are most concerned about. Across genders, the financial topics that employees reported seeking education or advice on included investing money in their retirement plan, how much to save for retirement, generating income in retirement, and building emergency savings, according to a December 2020 **report** by the Employee Benefit Research Institute (EBRI).

A 2020 **study** by Bank of America Merrill Lynch, however, found that financial wellness concerns can vary significantly by gender. Women were more than twice as likely to include paying off credit card debt among their top three goals, and only 33% of women reported feeling like they are in control of their debts compared with 51% of men.

In addition to tailoring financial wellness programs to women's priorities, other steps employers could implement to strengthen the financial preparedness of their female employees include:

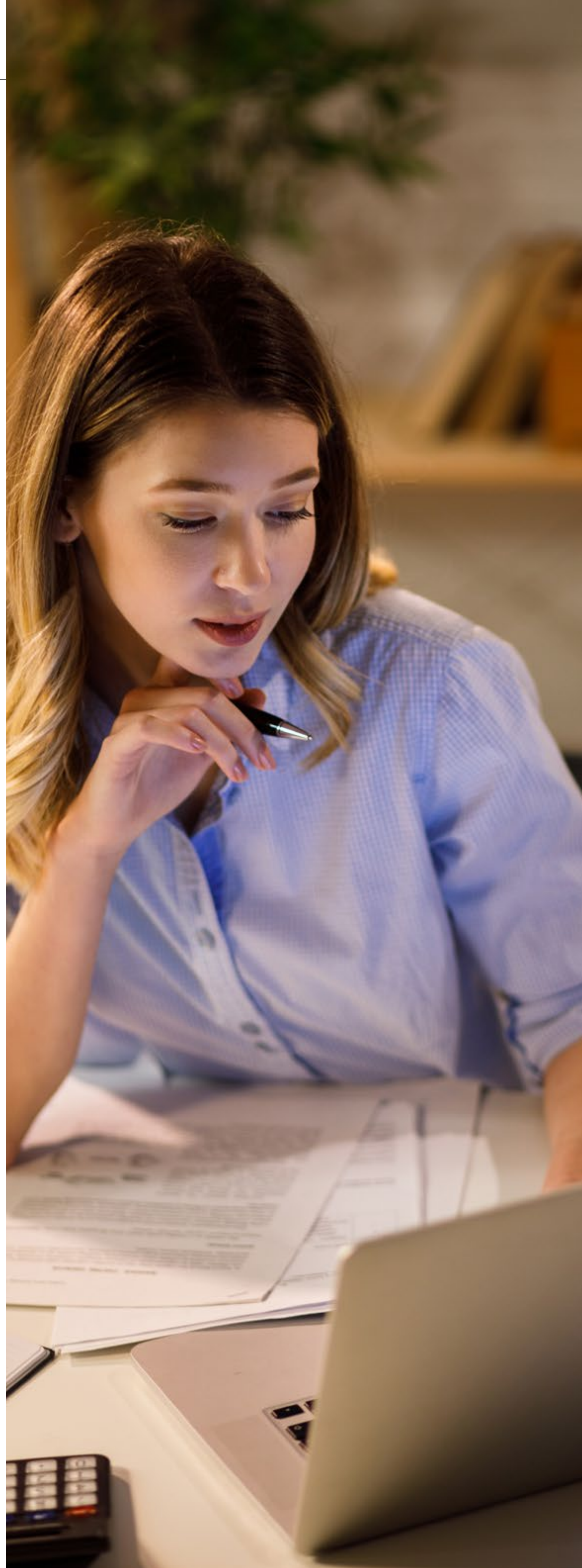
- Ask service providers about available financial wellness tools or partnerships with other vendors to offer financial wellness in their benefits lineup
- Increase communication efforts to ensure that employees know the resources and tools available to them including a consideration to make attendance to an educational meeting mandatory
- Extend retirement plan participation to qualified part-time workers
- Offer flexible work plans such as working from home or reduced hours for those with increased at-home caregiver responsibilities
- Consider offering phased retirement programs

BDO INSIGHT: ENCOURAGE FINANCIAL CONSIDERATIONS

Raising women's comfort levels in talking about financial issues can be a great first step for employers to prioritize in their financial wellness programs. The EBRI report found that women are significantly less likely (13%) than men (28%) to frequently discuss saving, investing, and planning with family and close friends, and women are significantly more likely (28%) than men (17%) to never discuss these topics.

Beyond simply providing valuable educational resources and expanding access to retirement plans, employers can make a major impact by offering opportunities for workers to talk about financial issues through women inclusion programs, lunch and learns, and other programs. A mentorship program included within a women's' inclusion program regarding financial issues amongst women would be helpful.

Your BDO representative is available to help you review available financial wellness programs and find those that are best for your workforce.



Consolidated Appropriations Act: What Plan Sponsors Need to Know About Retirement Plan Relief

The Consolidated Appropriations Act, 2021 (CAA), which was enacted on December 27, 2020, is mostly known for the $900 billion it provided in additional stimulus funding for pandemic relief. Additionally, the law contains several useful provisions for retirement plans, including non-COVID disaster emergency relief, multiemployer and defined benefit plan changes, and updates to partial plan terminations. All of these provisions are discretionary, and have very narrow applicability. Regardless, plan sponsors should take the time to understand the relevant parts of the law and see whether the various provisions might benefit their organizations and plan participants.

NON-COVID-RELATED DISASTER RELIEF

The CAA allows (but does not require) special retirement plan distributions for non-COVID major disasters (such as the 2020 Gulf Coast hurricanes and California wildfires) that occurred between December 28, 2019 and December 27, 2020 (the date the CAA was enacted), so long as the disaster declaration occurs no later than 60 days after the CAA was enacted. Participants whose principal residence was within the disaster area and who sustained an economic loss as a result of the disaster have until June 25, 2021 (180 days after the CAA was enacted) to receive these special CAA disaster distributions. It is important to note that this law does not extend disaster relief outlined in the Coronavirus Aid, Relief, and Economic Security (CARES) Act, but it does mirror aid offered for previous natural disasters. The law allows organizations to amend their 401(k), 403(b) or 457(b) plans to permit qualified participants living in the declared disaster area to obtain special relief using the following methods:

- **Disaster-related distributions:** Qualified participants in defined contribution retirement plans and individual retirement accounts (IRA) may take up to $100,000 out of their accounts for each separate disaster without incurring the 10% early withdrawal fee. Although such distributions are taxable, they may be repaid in full or in part over a three-year period beginning on the distribution date (and such repayments will be treated as rollover contributions).
- **Plan loan relief:** Similar to the CARES Act provision, participants can borrow the lesser of 100% of the vested account balance or $100,000 for each separate disaster.
- **Loan repayments:** Repayments on the aforementioned loans may be suspended for up to one year if the repayment of the loan would have normally been due on the first day of the disaster through 180 days after the last day of the disaster.
- **Recontribution of hardship distributions for home purchases:** Qualified participants who took a distribution to buy or reconstruct a home and were unable to use some or all of the funds can return those funds to their accounts. The funds must have been received no more than 180 days before and up to 30 days after the qualified disaster.

In general, plan sponsors interested in adopting all or some of these changes should amend their plans on or before the last day of the first plan year beginning on or after January 1, 2022.

MONEY PURCHASE PLAN DISTRIBUTIONS QUALIFY FOR COVID-RELATED DISTRIBUTIONS (CRDS)

The CAA reverses Internal Revenue Service (IRS) **Notice 2020-50**, which said in-service distributions from money purchase pension plans did not qualify as a CRD. The change may have come too late for plan sponsors that denied CRDs based on the IRS's initial notice, but it could reassure others who altered their plans to help participants.

RELIEF FOR OVERFUNDED PENSION PLANS

The Internal Revenue Code (IRC) Section 420 says plan sponsors with overfunded defined benefit plans can make a future transfer of that surplus to retiree health and/or insurance accounts. Because of market volatility over the past year, pension funding may have declined, so the CAA allows plan sponsors to reverse their planned, future Section 420 transfers.

IN-SERVICE DISTRIBUTIONS FOR SPECIFIC TRADE MULTIEMPLOYER PLANS

IRC Section 401(a)(36) provides incentives for phased retirement programs by allowing in-service distributions from multiemployer plans for active/working participants age 59½ or older. The CAA reduces this age requirement to 55 for participants in multiemployer plans from building and construction industries. One additional requirement: participants must have been in the plan on or before April 30, 2013.

PARTIAL PLAN TERMINATIONS

The CAA creates a safe harbor to protect plans that might otherwise experience a partial plan termination. Before, a partial plan termination would have generally occurred when 20% or more of employees participating in a defined benefit or defined contribution plan were involuntarily terminated from employment without full vesting during a plan year (or over several plan years). The CAA provides that if the number of active participants covered by the plan on March 31, 2021 is at least 80% of the number of active participants covered by the plan on March 13, 2020, the plan will not be treated as having a partial termination. The relief is based on the total number of active participants, so employers do not have to rehire the same workers who were laid off.

BDO INSIGHT:

The CAA offers many tools plan sponsors can use to help ease participants' financial strain. It is important to read the details in the law's provisions and pay attention to qualifications and deadlines. Plan sponsors interested in adopting any aspects of this relief should reach out to the plan's service providers to see whether immediate adjustments are needed to existing plan processes.

BDO's professionals can **examine retirement plans** and assist in determining whether the CAA provisions might benefit your organization's circumstances.

“Free” COBRA Group Health Care for up to Six Months for Involuntarily Terminated (or Reduced Hours)

The American Rescue Plan Act of 2021 (ARPA), enacted on March 11, 2021, creates a requirement that employers treat the total payment for Consolidated Omnibus Budget Reconciliation Act (COBRA) continuation coverage due from certain eligible individuals as being “paid in full” for April 1 through September 30, 2021 (Subsidy Period). The eligible individuals with COBRA coverage will not receive the subsidy directly from the government; rather, they will have a premium holiday during which time the employer pays 100% of the applicable COBRA premium. The employer will be reimbursed in full through refundable payroll tax credits.

COBRA gives workers and their families who are losing employer health care coverage the right to retain the coverage by paying a premium amount. The ARPA provisions do not apply to all COBRA-eligible individuals; eligibility is limited to employees who lost health care benefits due to an involuntary termination or reduction in hours. While the loss of coverage event can be linked to COVID-19, it is not required to be. A loss of coverage event could have occurred as far back as November 1, 2019, since the law requires an employer to offer a continuation of COBRA coverage for 18 months after an involuntary termination (18 months from November 1, 2019 is April 30, 2021). Eligible individuals who opted not to pay for COBRA coverage will be given another opportunity to elect the free coverage.

Employers and COBRA administrators should prepare to distribute new COBRA election and subsidy notices and to make operational changes soon after further guidance is released. Eligible individuals who are not already on COBRA will need to act quickly after receiving the notice to elect subsidized COBRA coverage. Failing to timely elect COBRA coverage could result in forfeiting this valuable benefit.

It is expected that many people will rush to take advantage of this opportunity, which can provide up to six months of health insurance at no cost. However, employers should keep in mind that the subsidy is available only for certain limited situations.

WHICH EMPLOYERS ARE ELIGIBLE FOR THE NEW SUBSIDY?

Employers who are subject to federal COBRA provisions or to a state program that provides comparable group health care continuation coverage are not allowed to charge eligible individuals for COBRA coverage during the Subsidy Period. The subsidy applies to workers in every industry, most tax-exempt employers (except churches who are exempt from COBRA) and union, governmental and Indian tribal government workers. The federal COBRA provisions generally apply to all private-sector group health plans maintained by employers that had at least 20 employees on more than 50% of its typical business days in the previous calendar year. Both full- and part-time employees are counted to determine whether a plan is subject to federal COBRA coverage. Many states have “mini-COBRA” laws that apply to employers who have fewer than 20 employees. The subsidy is mandatory for all employer-sponsored group health plans (i.e., all employers must offer the subsidy, regardless of whether the plan is fully or partially insured, or self-insured).

During the Subsidy Period, generally, the federal government will reimburse COBRA costs to employers by allowing credits against employers’ Medicare (not Social Security or income) taxes (but for union plans, the plan would receive the subsidy and for insured, state “mini-COBRA” plans, the insurer would receive the subsidy). Guidance is needed to clarify how the flow of funds for the subsidy would work. The full cost of COBRA continuation coverage (including up to a 2% administrative fee) at any coverage level (e.g., single, “single-plus-one” or family coverage) for employees and former employees and their spouses and dependents is eligible for the subsidy via the payroll tax credit. The subsidy applies to health, prescription drug, dental and vision plans, but does not apply to health flexible spending accounts (FSAs), health savings accounts (HSAs) or long-term care plans (further guidance is needed to clarify the scope of the subsidy).

Due to the fact that most individuals who elect COBRA group health care continuation coverage usually pay 100% of those premiums (and in many cases they must also pay up to a 2% administrative fee), the new subsidy via the employment tax credit keeps the free COBRA coverage at zero cost to the employer. While the employment tax credit is taxable income, it will be offset by the employer's deductible payment of the healthcare premiums.

IMPACT ON ELIGIBLE INDIVIDUALS

An eligible individual with an existing or new COBRA election will be provided tax-free health care coverage (both the premium and any administrative charge) at no charge for their remaining COBRA period that overlaps with the Subsidy Period.

The free COBRA provided during the Subsidy Period would be "affordable" coverage under the Affordable Care Act (ACA). But it is not clear how this "affordable" coverage affects an individual who has purchased coverage on the exchange before they had an offer of affordable coverage.

A recipient of the free health care coverage must notify the employer or plan administrator when they become eligible for Medicare or another group health plan—other than coverage under an excepted benefit, an FSA or a qualified small employer health reimbursement arrangement (QSEHRA). Individuals who fail to promptly give this notice could be subject to a $250 fine and other penalties.

WHO IS ELIGIBLE?

Generally, individuals are eligible for free COBRA coverage if (1) they are involuntarily terminated or have a reduction in hours that qualifies them for federal or state COBRA coverage and (2) the Subsidy Period overlaps with their COBRA coverage period.

The new COBRA premium assistance is not available to the following individuals:

- Employees who are terminated for gross misconduct.
- Employees who voluntarily terminated their employment or who retired.
- Individuals who are eligible for COBRA due to other reasons, like divorce, death or loss of dependency status.
- Individuals who are eligible for other group health care coverage (such as from a new employer) or Medicare.
- Individuals who are beyond their normal COBRA coverage period connected to the original qualifying event (i.e., the employee's involuntary termination or reduction in hours that caused a loss of group health plan coverage).
- Domestic partners who are not federal income tax dependents of the employee.

WHAT'S THE COVERAGE?

Generally, the COBRA coverage will be the same as the coverage elected just prior to the involuntary termination or reduction in hours. However, employers can (but are not required to) allow individuals who are eligible for premium assistance to change their coverage provided it does not result in an increased premium cost. Further guidance is needed regarding the scope of who can change to a lower cost health plan as a result of the new law.

Eligible individuals who lost health care coverage after October 31, 2019 but do not have COBRA coverage on April 1, 2021 due to nonelection or lapse of payment will have a new, 60-day opportunity to elect COBRA coverage. If timely elected, the COBRA covered period will begin on the date of the individual's qualifying event, but it appears that no payment is due for months prior to April 2021 and no claims can be filed prior to April 1, 2021. For the months remaining in the COBRA period that coincide with April 1 through September 30, 2021, the employee makes no payment but will have claims paid in accordance with the plan's provisions. To have continued coverage after September 30, 2021, the employee must make the payments required under the plan. If the individual finds this unaffordable, they can simply drop the coverage.

BDO INSIGHT:

Consider the following example. An employee who was involuntary terminated on December 1, 2020 but did not elect COBRA coverage at that time would be eligible for 100% subsidized COBRA coverage from April 1 through September 30, 2021 and could continue self-paid COBRA coverage afterwards, for a total of 18 months of COBRA coverage measured from December 1, 2020.

But if an employee already had COBRA coverage for 15 months on March 30, 2021, then that employee would only be eligible for three more months of COBRA coverage (April, May and June 2021) and would be entitled to the subsidy for only those three months. Unless that employee has another COBRA-qualifying event during the original COBRA coverage period (such as becoming disabled), that employee would not be entitled to any COBRA coverage thereafter (so that employee would not qualify for the subsidy in July, August and September 2021, even though the coverage is "free" during those months).

It appears that an individual whose COBRA qualifying event was earlier than April 1, 2021 can elect COBRA starting on April 1, 2021 (and get the subsidy) and simply skip the period before April 1, 2021 if they did not need COBRA coverage for that earlier period of time. Such individual may also be offered a lower cost group health care option if the employer decides to offer that choice.

Since COBRA election deadlines have been extended due to COVID-19, many individuals may still be within their original COBRA election periods. This special COBRA election window allows these people to make a COBRA election for the period beginning on April 1, 2021 without having to pay premiums retroactively to their COBRA initial eligibility date. This is a significant departure from the regular COBRA rules. But the maximum COBRA coverage period is still counted from the date of the individual's original COBRA qualifying event.

WHAT NOTICES ARE NEEDED?

The federal government is expected to issue model required notices addressing the existence of the subsidy, the availability of the 60-day election period and advance notice of when the Subsidy Period will be ending. In the meantime, employers should prepare for the following new notice requirements.

Group health plans must modify their COBRA election notices for individuals who become eligible for federal or state COBRA during the Subsidy Period to notify them of the premium assistance (and, if applicable, the option to enroll in a lower priced plan).

By May 31, 2021, individuals who previously rejected (or terminated) COBRA coverage and to whom a new election period must be offered must be notified of their new election period and the availability of the premium assistance. This essentially creates a special COBRA enrollment period for such individuals.

Between August 17 and September 15, 2021, group health plans must provide a notice to individuals receiving the premium assistance stating that the subsidy will expire on September 30, 2021, and that they may be eligible for COBRA coverage without the subsidy. But if the subsidy would end earlier for any individual, the plan must provide a notice that the subsidy is expiring no earlier than 45 days and no later than 15 days before the subsidy expiration date.

It is not clear how these required notices must be delivered (sending paper mail to former employees may be needed).

HOW DOES THE SUBSIDY WORK?

Individuals who are eligible for COBRA premium assistance do not receive a payment from the federal government, group health plan, employer or insurer. Rather, their COBRA costs are waived during the Subsidy Period.

Employers that sponsor a fully-insured plan would continue paying the full premium to the insurer for the assistance eligible participants. Employers that sponsor a self-insured plan would pay the claims incurred by the assistance eligible participants. In both cases, the employer would receive no payment from the eligible individual during the Subsidy Period but would instead recover its COBRA costs (102% of the COBRA premium) for the assistance-eligible individuals by claiming a refundable federal tax credit against the employer's Medicare taxes.

The COBRA subsidy is prospective only and cannot begin before April 1, 2021.

Although the law does not require employers to pay for any COBRA coverage, some employers pay for some or all of COBRA coverage (for example, as part of a severance package). Such employers can cease those contributions during the Subsidy Period and the federal government will provide the subsidy for 6 months. And although the subsidy is tax-free to employees, employers who take the COBRA premium tax credit must increase their gross income by the amount of such credit for the taxable year which includes the last day of any calendar quarter with respect to which such credit is allowed.

Also, under a "no double dipping" rule, employers cannot take the COBRA premium tax credit for any amount which is taken into account as qualified wages for the employee retention credit (ERC) under the Coronavirus Aid, Relief, and Economic Security Act and Consolidated Appropriations Act, 2021 (CAA), or as qualified health plan expenses for the Families First Coronavirus Response Act (FFCRA), as amended by CAA and ARPA. Likewise, amounts attributable to the COBRA premium tax credit would not be eligible payroll costs under the Paycheck Protection Program (PPP).

Guidance from the Internal Revenue Service (IRS) is needed to clarify how exactly employers would claim the tax credit, but it appears that employers would claim the credit on their quarterly IRS Form 941 or in advance on IRS Form 7200 if the actual or estimated amount of the credit exceeds the employer's Medicare taxes for any calendar quarter. Further guidance is also needed regarding the mechanics of the subsidy for employers that have insured state COBRA coverage, since under Section 9501(b) of the ARPA the tax credits reimbursements would go to the insurer, not the employer.

BDO INSIGHT:

For past COVID-19 relief tax credits, such as the ERC and FFCRA, IRS guidance allowed employers to dip into withheld income and Social Security taxes as a source of claiming those refundable tax credits. But the IRS has not yet authorized such actions for the ARPA COBRA subsidy tax credit. Social Security taxes may not be available as a source for the new COBRA tax credits, since the ARPA was enacted under budget reconciliation rules which prohibit any changes to Social Security.

Employers are not allowed to voluntarily expand the group of people who are eligible for the special COBRA premium subsidy, because the federal government is paying the full COBRA premium for the designated class of assistance-eligible individuals.

We expect the IRS to issue FAQs on the new COBRA Medicare tax credits, similar to the FAQs that the IRS issued on the ERC and FFCRA payroll tax credits.

This new COBRA subsidy may be economically more valuable than using qualified health care expenses for the ERC, because ERC nets 70% on the dollar whereas the COBRA subsidy is 102% (premium plus administrative charge).

WHAT SHOULD EMPLOYERS DO NOW?

Employers should immediately identify all employees who lost group health plan coverage after October 31, 2019 due to an involuntary termination or reduction in hours, without regard to their COBRA elections, because such event would have entitled the individual to 18 months of COBRA coverage (i.e., through April 30, 2021). Guidance is needed on whether notices must be given to individuals in this group that declined COBRA due to eligibility in another employer's plan or Medicare. Employers will need to notify individuals who have an unexpired COBRA period that premium assistance is available, and they have a right to reconsider their original COBRA election.

Employers will also need to review and perhaps modify any existing, automatic processes that might otherwise terminate COBRA coverage when premiums are not received during the Subsidy Period.

Year-end reporting on health benefits should also be reviewed to ensure these increased COBRA participants receive the appropriate Form 1095-B or C for 2021.

Employers should develop a procedure to identify COBRA recipients who are eligible for the premium assistance and those who do not qualify (for example, employers will need to distinguish a voluntary quit from an involuntary termination of employment and whether the employee was fired for gross misconduct). For premium-assistance eligible individuals, employers must refund within 60 days any premiums paid during the Subsidy Period. Not all COBRA participants will qualify for the subsidy, so the plan administrator will still need to handle some premium payments from non-eligible individuals.

BDO INSIGHT:

Many employers use outside service providers for their COBRA administration, so employers should reach out to their vendors as soon as possible to coordinate their response to the ARPA changes to current COBRA rules, especially the special election period for certain assistance-eligible individuals.

Keep in mind that, separate from the ARPA COBRA subsidy, many employees (and their family members) may currently have extended COBRA election rights due to COVID-19 deadline extensions. For example, **ERISA Disaster Relief Notice 2021-1** issued on February 26, 2021, announced an individualized one-year deadline extension for COBRA elections, which begins on the date the clock for the particular deadline would have started running (i.e., the one-year extension is applied on a rolling basis to each deadline for each affected individual). But individuals electing retroactive COBRA coverage under those extended deadlines will generally have to pay the full COBRA premiums for such periods. Guidance is needed on how the deadline extension coordinates with the new COBRA subsidy.

Employers may recall that in February 2009, under the American Recovery and Reinvestment Act of 2009 (ARRA) (when President Biden was then Vice President Biden), the federal government subsidized 65% of COBRA premiums for certain individuals who were terminated or laid off between September 1, 2008 and March 31, 2010 due to the financial crisis linked to the bursting of the home mortgage lending bubble. The ARRA subsidy was extended through May 31, 2010, so perhaps with Democrats currently controlling both Congress and the White House, the ARPA COBRA subsidy may be extended beyond September 30, 2021. Also, the ARRA may be a model for how the flow of funds will work for the ARPA premium tax credits for insured state COBRA coverage.

Hardship Distributions: What Plan Sponsors Need to Know About Complying with Recent Changes

Efforts to keep up with the myriad of challenges that retirement plan sponsors faced in 2020 may have caused some to overlook significant changes related to hardship distributions that were enacted before the onset of the COVID-19 pandemic.

These changes are designed to make it easier for participants to access funds from their 401(k) plans if they are experiencing significant financial hardship, and several changes apply to 403(b) plans as well. Some of these provisions were optional from 2018 to 2019 but became mandatory in 2020 for plan sponsors that chose to allow hardship distributions.

Now is the time for plan sponsors to examine whether they are complying with these changes in how they administer their plans and whether their plan documents accurately reflect these changes.

BACKGROUND ON HARDSHIP DISTRIBUTION RULE CHANGES

Plans are allowed—but not required—to offer taxable, in-service hardship distributions to participants who demonstrate an "immediate and heavy financial need" that could be satisfied only by taking money from their retirement accounts. In the past, that need was determined by facts and circumstances and certain safe harbors built into the law.

Over the past several years, legislation (e.g., the Tax Cuts and Jobs Act of 2017 and the Bipartisan Budget Act of 2018) and Internal Revenue Service (IRS) regulations have introduced changes to make it easier for participants to withdraw funds from their accounts via hardship distributions.

SIGNIFICANT HARDSHIP DISTRIBUTION PROVISIONS NOW IN EFFECT

The most significant changes related to hardship distributions that are now in effect include:

- **Elimination of six-month suspension on contributions (mandatory):** Previously, plan sponsors were required to suspend participant contributions for six months after the participant took a hardship distribution. Some plan sponsors viewed this suspension as a way to help participants seriously consider the consequences of taking a distribution on their retirement savings, and not view their 401(k) as an ATM. For hardship distributions made on or after January 1, 2020, plan sponsors cannot impose the six-month suspension and must allow participants to immediately contribute to their retirement accounts. This change was optional in 2019 but became mandatory in 2020.
- **Expanded safe harbors (mandatory):** To determine whether participants qualify for hardship distributions, plans can use the hardship safe harbor test and/or the hardship facts and circumstances without regard to any safe harbors. Many plans include both options for maximum flexibility. Previously, there were six safe harbors that plan sponsors could use to determine whether participants qualify for hardship distributions; these safe harbors were available if the participant needed funds to pay for medical expenses, home purchases, college tuition, funeral expenses and home casualty repairs, as well as to prevent eviction or foreclosure. The new rules add a seventh safe harbor to this list: disaster-related expenses of participants who live in a federally declared disaster area. Plan sponsors had the option of including this as a safe harbor in 2019, but its inclusion became mandatory in 2020.

- **Three-part test replaces some facts-and-circumstances determinations (mandatory):** Previously, plan sponsors had to evaluate certain facts and circumstances to determine whether a participant qualified for a hardship distribution. For hardship distributions made on or after January 1, 2020, the new rules allow employees to self-certify that: 1) distributions do not exceed the amount the employee needs; 2) participants exhausted other resources, including deferred compensation; and 3) participants do not have reasonably available assets to take care of their needs.
- **Elimination of loan requirement (optional):** Previously, participants had to have taken the maximum allowed loans from their plans before being allowed to permanently withdraw funds via a hardship distribution. Now plan sponsors can—but are not required to—allow participants to take a hardship distribution without first having to take a loan.
- **Expanded sources of funds for hardship distributions (optional):** Plan sponsors now can—but are not required to—allow hardship distributions to be made from Qualified Non-Elective Employer Contributions (QNECs), Qualified Matching Contributions (QMACs), and traditional and Qualified Automatic Contribution Arrangement (QACA) safe harbor contributions and earnings.

Your BDO representative can help examine your plan to determine whether it needs amendments to its hardship distribution process and plan document.

BDO INSIGHT: ENSURE OPERATIONAL AND PLAN DOCUMENT ALIGNMENT BEFORE DECEMBER 31, 2021 DEADLINE

Plan sponsors need to be aware that some of the changes discussed above were optional in 2018 and 2019 but became mandatory in 2020, while others remain optional. This creates a confusing situation for plan sponsors as they work to comply with these changes—especially amid all of the other changes related to the pandemic.

Regardless, plan sponsors need to understand the hardship distribution-related changes and comply with them, both in terms of how they operate their plans and how they are reflected in the plan document. Plan sponsors have until December 31, 2021 to amend their documents to reflect these changes. In addition, it is important to notify participants about these changes.

Plan sponsors, even those that use preapproved plans, should meet with their service providers and advisors to review the current plan operations and plan document to identify any areas that are not aligned with the new rules. Lastly, while it is better to bring the plan in compliance as soon as possible, the IRS also has its Employee Plans Compliance Resolution System to fix errors found in retirement plans.

Correcting Potential Errors Relating to CARES Act Loans

During the first year of the COVID-19 pandemic, Congress provided plan sponsors with a broad toolkit to help employees access retirement assets and manage loan repayments. However, many of the provisions associated with retirement plan loans in the Coronavirus Aid, Relief and Economic Security (CARES) Act have now expired. Plan sponsors should work with their service providers to ensure that loans are being administered accordingly—or take advantage of federal self-correcting programs to get retirement plan loans back on track.

REVIEW OF CARES ACT LOAN PROVISIONS

The CARES Act allowed employers to increase the amount participants could borrow from their 401(k), 403(b) or 457 plans. Previously, the limit was the lesser of $50,000 or 50% of the vested balance, but during the period March 27, 2020 to September 22, 2020, participants with a valid COVID-19-related reason could borrow the lesser of $100,000 or 100% of the vested balance.

A second provision allowed participants to suspend repayments on any outstanding plan loan between March 27 and December 31, 2020 if they were affected by the pandemic. The CARES Act also extended the repayment term for loans (usually five years) by an additional year. Repayment schedules needed to be re-amortized (including interest incurred during the suspension of repayments) and resumed in January 2021.

POSSIBLE ERRORS—AND HOW TO CORRECT THEM

The CARES Act included many moving parts and different deadlines related to loans. As a result, many plan sponsors—or their third-party service providers—may have made errors related to participant loans, including missing important cutoff or restart dates. For example, many 401(k) loans are initiated by the participant electronically and often solely through the service provider's platform—not through the employer. It is possible that some of these service providers may have continued making loans up to the higher CARES Act limits after the September 22, 2020 deadline. Similarly, service providers may not have properly re-amortized loans that were suspended during the nine-month period allowed by the CARES Act (using the outstanding principal and accrued interest), and some participants may not have resumed making repayments at the beginning of 2021.

Plan sponsors should review IRS **Notice 2020-50**, which explains the qualifications and deadlines for CARES Act loans. If an error is discovered, the IRS and the Department of Labor (DOL) have correction programs that can help plan sponsors correct errors and avoid disqualification and/or severe penalties.

The IRS's **Employee Plans Compliance Resolution System** (EPCRS) offers three ways to resolve problems; the level of plan failure determines the route employers need to take to resolve the issue. In addition, employers may need to address errors using the DOL's **Voluntary Fiduciary Correction Program** (VFCP). This self-correction program addresses 19 different prohibited transactions, including participant loans that fail to comply with plan provisions for amount, duration or level of amortization.

BDO INSIGHT: FIDUCIARY DUTY ULTIMATELY FALLS ON PLAN SPONSOR

Part of a plan sponsor's fiduciary duty is to select service providers wisely and monitor whether they are complying with the plan document and existing laws. Most service providers disavow fiduciary status, so, in many cases, the employer is ultimately responsible for ensuring that the plan operates in compliance with its terms and applicable law. Failure to fulfill this responsibility could lead to severe consequences.

Plan sponsors should review participant loans and work with service providers to ensure that the loan process has been managed in accordance with the changing federal guidelines. If plan sponsors discover an error, they should document the issue as thoroughly as possible (including how the pandemic may have contributed to the oversight) and turn to the IRS and DOL self-correction programs.

SAS 136: What Plan Sponsors Need to Know About Upcoming Changes to ERISA Plan Audits

Employee benefit plan sponsors and their auditing firms need to begin preparing for the adoption of Statement on Auditing Standards No. 136 (**SAS 136**), Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA (Employee Retirement Income Security Act of 1974). This auditing standard was enacted by the American Institute of Certified Public Accountants (AICPA), and was effective for years ending after December 15, 2020. While the AICPA delayed the effective date by one year due to the COVID-19 pandemic, auditing firms may choose to adopt the standard on the original effective date. Plan sponsors will need to take the time to understand SAS 136 and its effect on the audit process.

GOALS OF SAS 136

In 2015, the Department of Labor's Employee Benefits Security Administration (EBSA) examined the quality of audit work done on employee benefit plans by independent qualified public accountants. SAS 136 is the AICPA's effort to address some of the issues found in the EBSA examinations.

The goal of SAS 136 is to enhance the quality of audits of ERISA plans by prescribing certain procedures that are required to be performed in the audit. The auditing standard also looks to add transparency to the nature and scope of ERISA benefit plan audits as presented in the auditor's report.

CHANGES TO AUDIT REPORTS, ENGAGEMENT LETTERS AND OTHER COMMUNICATIONS

SAS 136 clarifies the responsibilities of plan management and auditors. Certain of these responsibilities are now included in the auditor's report, engagement letters and required communications.

The auditor's responsibilities are now disclosed in the auditor's report which include professional judgements, professional skepticism and the auditor's communication with those charged with governance. Management's responsibility to maintain a plan instrument, administer the plan, maintain sufficient records for plan transactions and benefits, and their responsibility for the financial statements are not stated in the auditor's report however will be stated in the engagement letter with their plan auditor. Management's responsibility for the assessment of going concern and the auditor's responsibility over management's assessment is also included in the auditor's report, when applicable.

The overriding goal of these changes is to clarify each party's role and responsibility throughout the audit process and formalize certain procedures that in the past were sometimes left to auditor's judgement.

Under the new standard, plan sponsors can expect to see a more thorough audit report. SAS 136 changes how auditors report their findings to those charged with governance. In addition to communicating deficiencies in internal control, auditors will now also have to communicate reportable findings in writing to those charged with governance.

CHANGES TO AUDIT PROCEDURES AND DOCUMENTATION

SAS 136 implements changes that affect multiple aspects of an ERISA plan audit, including engagement acceptance, risk assessment and response, communication with those charged with governance, and performance procedures and reporting.

Some of the most notable changes include:

- If a plan sponsor elects an ERISA Section 103(a)(3)(C) – formerly known as a limited scope audit – management must affirm that this is permissible and that the qualified institution can certify the investment information
- Management must provide to the auditor a substantially complete Form 5500 draft before issuance of the auditor's report
- The auditor must communicate reportable findings

CHANGE IN LIMITED SCOPE AUDITS

Before SAS 136, plan sponsors could elect to have a limited scope audit performed, which excludes certain audit procedures over investments and investment income that are certified by a qualified institution as complete and accurate. SAS 136 eliminates the limited scope moniker and replaces it with an ERISA Section 103(a)(3)(C) audit, which includes heightened reporting requirements.

BDO INSIGHT: GEAR UP FOR EARLY ADOPTION

Even though SAS 136's effective date is for periods ending on or after December 15, 2021, some accounting firms, including BDO, have chosen to adopt the new standard this year. The earlier plan sponsors start discussing the upcoming changes with their audit team, the better prepared they will be to understand and fulfill responsibilities during the plan audit.

To learn more about how SAS 136 will change the communications, deliverables and responsibilities related to ERISA plan audits, please contact your BDO representative.

Practical Matters: FAQs for Plan Sponsors and Employees on CARES Act Relief

The Coronavirus Aid, Relief and Economic Security (CARES) Act was a rapid response by the federal government to help businesses and employees cope with the economic issues caused by the pandemic. Many aspects of the wide-range law make significant changes affecting employer-sponsored retirement plans and their participants.

Since Congress passed the CARES Act in March 2020, BDO has received numerous questions from plan sponsors about the law's impact on plans and participants. Below is a list of some of the most common questions plan sponsors face, along with our brief answers.

1. DID COVID-19 FURLOUGHS CREATE PARTIAL PLAN TERMINATIONS?

If an employer furloughed a significant portion of its workforce because of COVID-19 or the resulting economic downturn, it is possible that those furloughs triggered a partial plan termination. A **partial plan termination** happens generally when 20% or more of participants terminate employment without full vesting during a particular year. Partial terminations can occur in connection with a significant corporate event such as a plant closing, or as a result of general employee turnover due to adverse economic conditions or other reasons that are not within the employer's control. A furlough is an involuntary, unpaid temporary leave, but the individual is still considered an employee. A furloughed employee would generally not be considered in the calculation for a partial plan termination as long as the employee returns to work within the plan year. Determining whether a partial plan termination occurred requires plan sponsors to calculate the turnover rate as well as take a careful look at the facts and circumstances surrounding the action(s). There is no one perfect formula that fits all situations.

Plan sponsors now have until March 31, 2021 to return the size of their workforces to a level that would avoid a partial plan termination.

2. IF YES, DO PLANS SPONSORS HAVE TO VEST EVERYONE OR JUST THE FURLOUGHED WORKERS?

When a partial plan termination does occur, affected employees (i.e., those who have been terminated) automatically become 100% vested in all employer contributions, including matching contributions. Please visit our plan termination **article** for more information.

3. WHEN DO PLAN SPONSORS APPLY THE PARTIAL TERMINATION RULES?

The applicable period depends upon the plan's circumstances, but it usually takes place during a specific plan year; the timeframe may be extended to more than one plan year if there are multiple, related severance events. See the Internal Revenue Service's (IRS) **issue snapshot** on partial plan terminations.

4. ARE SICK LEAVE AND FAMILY LEAVE PAYMENTS THAT ARE MANDATED BY THE FAMILIES FIRST CORONAVIRUS RESPONSE ACT (FFCRA) TREATED AS PLAN COMPENSATION?

Probably yes, since FFCRA paid time off would be included in Box 1 of Form W-2 and many retirement plans define "compensation" as including Box 1, W-2 compensation. But plan sponsors will need to look at how their plan defines "compensation." If paid time off is excluded, then FFCRA paid time off would likewise be excluded (but such exclusion seems to be rare).

5. WHY ARE AUDITORS ASKING PLAN SPONSORS TO DOCUMENT THEIR GOING CONCERN POSITIONS IN A MEMO?

Many plan sponsors are unsure of their ability to fund Employer contributions to their plans and have made changes to plans as a result of the pandemic. As outlined in FASB ASU 2014-15, the responsibility for performing the annual going-concern assessment is placed on management. It is critical for management to prepare this analysis for their financial statements, including a memo on their considerations. The memo helps auditors evaluate whether there is substantial doubt about the plan's ability to continue as a going concern. This formerly was the auditor's responsibility, but in the past five years, this has shifted and is now a standard duty of the plan sponsor.

6. WHAT ARE THE MOST COMMONLY ADOPTED PROVISIONS FROM THE CARES ACT?

According to research from Plan Sponsor Council of America, 46% of surveyed plans have elected to allow repayment of coronavirus-related distributions during the next three years, followed closely by 45% allowing some distributions until December 31, 2020. Only 9% of those surveyed adopted or plan to adopt no provisions.

7. WHAT IS THE DIFFERENCE BETWEEN "TEMPORARY IMPAIRMENT" AND "OTHER THAN TEMPORARY IMPAIRMENT"?

These are accounting principles used to describe the nature of the decrease in an asset's value, which is a standard topic that needs explanation in the plan's audit. "Temporary impairment" refers to normal market fluctuations in a specific investment; "other than temporary impairment" refers to a permanent decline in the investment with little to no chance of recovery. Given the extraordinary nature of the COVID-19 pandemic and its varying economic impact across industries and businesses, it is important to work with auditors to determine the correct classification of losses.

8. HOW CAN PLAN SPONSORS CHANGE THE TIMING AND FREQUENCY OF THE EMPLOYER MATCHING CONTRIBUTION FROM EACH PAY CYCLE TO A YEAR END CONTRIBUTION?

There are IRS and plan document limitations related to changes in certain types of Employer contributions, such as Safe Harbor contributions. However, generally a sponsor can more easily change the timing of the deposit of those contributions into the plan, rather than change the formula and eligibility provisions of the Employer contribution. When cashflow is tight, consider funding the contribution on an annual, quarterly, monthly, or per payroll period basis to fit your needs. Employers generally have until the extended due date of their federal income tax return for that tax year to deposit Employer contributions into the retirement plan. Plan sponsors should check their plan documents (and summary plan description) to see if an amendment is needed to change the timing of when Employer contributions are made to the plan.

9. DO PLAN SPONSORS HAVE TO IMPLEMENT THE CARES ACT PROVISIONS FOR THE NEW DISTRIBUTION AND LOAN OPTIONS?

The CARES Act expanded current rules on coronavirus-related distributions and loans, increasing the amount affected participants can pull from their accounts as well as the time they can take to repay the money, if applicable to the transaction. It's important for plan sponsors to understand that the distribution and loan provisions are optional, as outlined in IRS **Notice 2020-50**. Plan sponsors should be aware that they may choose amongst the provisions and adopt the ones that they feel their participants would benefit from the most.

10. IF PLAN SPONSORS IMPLEMENT A CHANGE TO THEIR PLAN ALLOWED BY THE CARES ACT, WHEN SHOULD THE PLAN DOCUMENT BE AMENDED TO REFLECT THE CHANGE?

Plan sponsors are permitted to make the CARES Act options available immediately even before a written amendment is made to the plan document. The deadline to formally adopt the amendments has been extended to December 31, 2022 (for calendar years) or the end of the plan year starting in 2022 (for non-calendar years).

11. CAN PLAN SPONSORS STOP MAKING EMPLOYER CONTRIBUTIONS?

In general, plans can reduce or eliminate discretionary non-elective and discretionary matching contributions without needing to amend plan documents, but plan sponsors need to examine plan documents to make this decision. Note that plans operating as Safe Harbor plans face a different set of requirements. See the section, "Can plans reduce or eliminate matching contributions?" in this BDO **article** to learn more about these requirements and other options plan sponsors have for conserving cash during the pandemic.

12. CAN PARTICIPANTS STILL TAKE A REQUIRED MINIMUM DISTRIBUTION (RMD) EVEN THOUGH RMDS WERE WAIVED FOR 2020?

Yes, but only if the plan allows withdrawals. The CARES Act allows participants to waive the RMD for 2020, but the law does not prohibit participants from taking a withdrawal. First, check the plan document to see whether withdrawals are allowed; then, see whether the plan has relaxed withdrawal rules as a result of the CARES Act to determine maximum amounts.

The Long-Term Impact of CARES Act Loans and Distributions on Retirement Savings

The Coronavirus Aid, Relief and Economic Security (CARES) Act allowed plan sponsors to relax loan and distribution rules in 2020, giving participants greater access to funds during the pandemic. These provisions were implemented to provide relief as many employees do not have adequate short-term savings. Employee Benefit Research Institute (EBRI) has found that only one in five families has at least three months of liquid savings. Layoffs, furloughs and other circumstances caused by the pandemic have left many workers struggling financially, so naturally, many looked to their retirement accounts for relief. While this access has been a useful tool for many financially strained Americans, such loans and withdrawals could inflict long-term damage on their progress toward a successful retirement.

Employers have an important role to play in helping to ensure that the flexibility offered by the CARES Act is used to alleviate workers' short-term financial strains while minimizing the impact on their overall retirement strategy. Employers can do their part by carefully communicating how these withdrawals affect the amount that will be available to use in retirement and providing resources to assist in developing strategies to recuperate those funds.

CARES ACT ALLOWS FOR LOANS AND CORONAVIRUS-RELATED DISTRIBUTIONS

Under the CARES Act, plan sponsors had the option to allow participants to take advantage of increased loans with delayed repayments or coronavirus-related distributions (CRDs) without an early withdrawal penalty. Participants are allowed – but not required – to pay back the distributions within three years. During 2020, employers determined whether they would allow those provisions to be adopted within their plans, and if so, the amounts in which employees could take.

Research from the Plan Sponsor Council of America (PSCA) found in the 4th quarter of 2020, 54% of plan sponsors adopted the provision to allow CRDs while 31% permitted an increase to the plan loan limit. When offered both the option of loans and CRDs under the CARES provisions, 54% of participants selected a CRD which would not require a repayment.

According to Vanguard, as of the end of 2020, only 5.7% of the participants offered the option to withdraw assets initiated a CRD. While the percentage of participants who selected this option is relatively low and is less than initially projected, the average distribution represented 55% of the participant's total balance with one in four distributions accounting for nearly 100% of their account balance. These participants may now face hardship in beginning their retirement savings accounts back at square one.

COMMUNICATE LONG-TERM IMPACT IN REAL TERMS

Plan sponsors who did adopt these provisions should help participants understand that loans and distributions from defined contribution plans can negatively affect retirement savings and help them build a strategy around getting back to where they were. Participants have a lot on their minds today; in addition to navigating the pandemic and work and childcare routines, many are also wrestling with financial issues like healthcare bills or mortgage payments. Providing educational resources can help show participants how they can rebuild savings and get back on track for retirement – including tangible examples of repayment schedules.

The Employee Benefit Research Institute (EBRI) created projections to show the impact of taking CRDs on employees' retirement balances for various age groups. These projections assume that employees take the full $100,000 distribution (or their full vested amount if it is less than $100,000). The projections show how much an employee's retirement account balance at age 65 is projected to decrease as a multiple of the employee's projected annual compensation at age 65.

In one scenario projected by the EBRI, employees take the full CRD and pay it back over three years. EBRI found that doing so caused account balances upon reaching age 65 to decrease a median of 2.3 percent across all age groups. But the negative impact was more than twice as significant (5.8 percent) for employees who took the distribution between the ages 60 and 64.

In another scenario, employees take the full CRD but do not pay it back. EBRI found that doing so caused account balances upon reaching age 65 to decrease a median of 20 percent for all age groups. But the negative impact was a staggering 45 percent for employees between the ages of 60 and 64.

BDO INSIGHT: HELP PARTICIPANTS SEE THE IMPACT

Based on the PSCA research, as of November 2020, only 38% of organizations had communicated the impact of these loans and distributions to plan participants. Plan sponsors can help their employees by providing straightforward information about how accessing the funds now can affect their financial futures. This information should include reminding participants that the repayment of these CRDs within the three-year time period will allow participants to avoid paying income taxes on the related distributions.

Although participants may not have the resources to currently increase their deferral rate to help make up the funds distributed as the pandemic is ongoing, plan sponsors should continue to encourage those who took CRDs to set a plan to increase their contributions in the future. Once financially stable, these participants can benefit from putting a plan in action to increase their contributions to make up for the funds and related investment earnings lost during this time period.

If you are trying to craft a clear communication strategy for your workforce on the impact of loans and distributions, your BDO representative is ready to help.

The Fallacy of the December 31 Closing for ESOP Transactions

While many businesses and their owners wish to close an Employee Stock Ownership Plan (ESOP) transaction by or on December 31, the importance of doing so can be overstated.

Many businesses and business owners contemplating a sale, merger or other liquidity event, oftentimes view closing a transaction before the end of the calendar year as important for a variety of tax and non-tax reasons, and ESOP transactions are no exception. As more and more companies discover the advantages of employee ownership, the number of new ESOP transactions closing on or just before December 31 continues to grow.

WHY DO YEAR-END CLOSINGS SEEM LIKE A GOOD CHOICE FOR ESOP TRANSACTIONS?

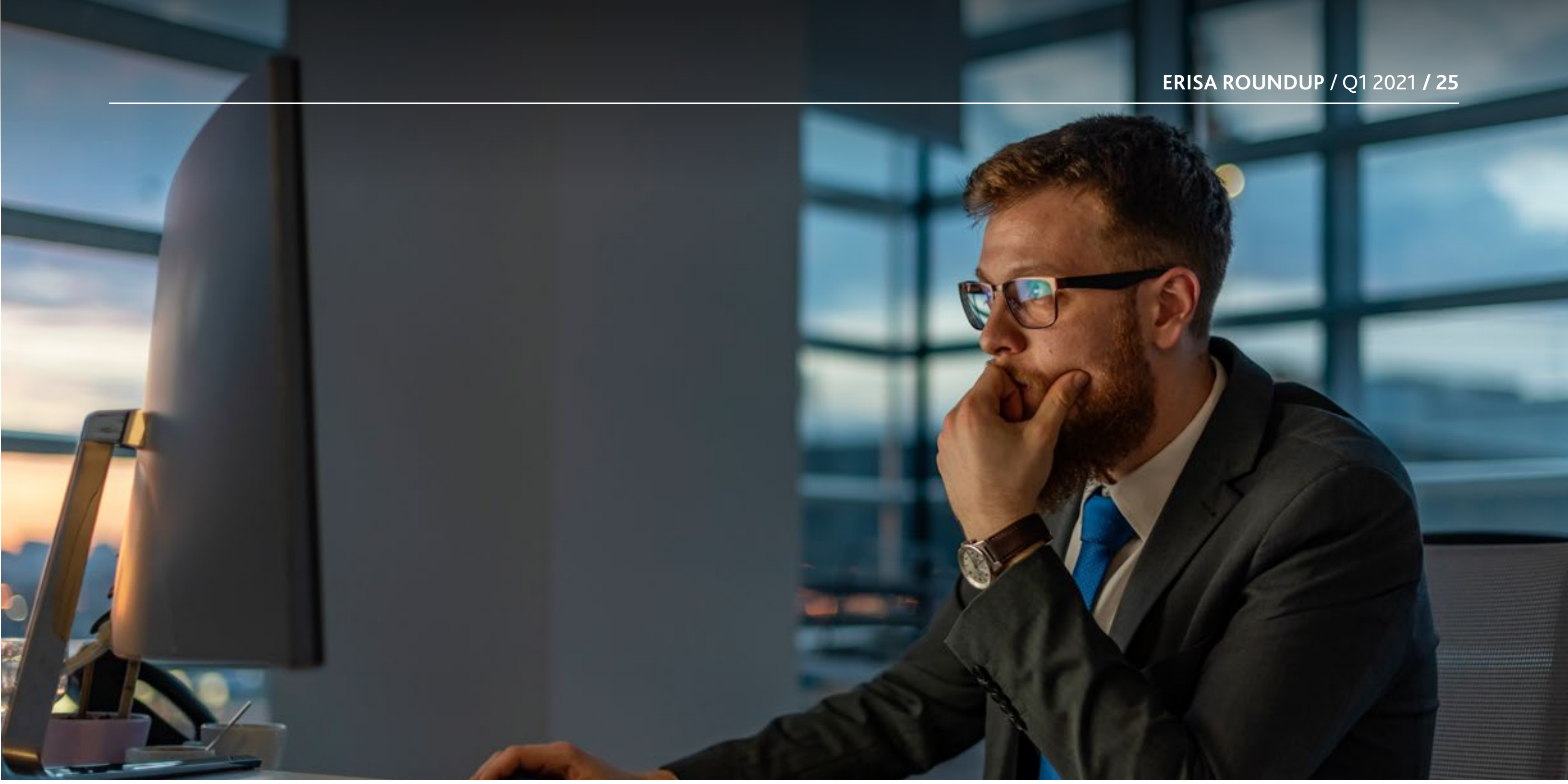
There are a handful of factors that make a year-end close popular. The first, and perhaps most common, is that closing an ESOP transaction at the end of the year starts off the new year with a "clean slate" as an ESOP-owned company and seems tidier from a bookkeeping perspective. Second, closing an ESOP transaction before year-end may permit a company to make a contribution to the ESOP in that fiscal year, allowing for some shares to begin to flow into participants' accounts, and in most cases, providing the company with a beneficial income tax deduction. However, these advantages should not be the determining factor in deciding when to close the transaction.

While a year-end close may seem tidy from an accounting perspective, it also is very common for transactions to close on a month-end, which can make for a convenient cut-off date as with a year-end close. As always, from a business perspective, the decision to sell a business should be strategic in nature first and foremost, with the accounting of the transaction playing an important, but secondary, role.

WHAT HAPPENS IF AN ESOP SALE OCCURS ON A DAY OTHER THAN YEAR-END?

If a sale occurs on a day other than year-end, the structure of the transaction will determine whether multiple tax returns need to be filed. Even if multiple tax returns are required, the time and cost of doing so are minimal compared to the results of a successful and well-planned transaction.

For the acquisition of C or S corporation stock by an ESOP, a change in ownership could limit the availability of tax attributes that might otherwise exist (i.e., **net operating losses** and tax credit carryforwards) but it should not result in a closing of the tax year for income tax purposes. If an S election is desired following the sale to an ESOP, there is a five-year restriction under Section 1362(g) that prevents a reelection to Subchapter S status if such status was terminated to take advantage of Section 1042 to allow for a tax-free shareholder rollover of proceeds into qualified replacement securities. However, if the company was a C corporation from inception, or for at least the last five years, and the sale occurs on December 31, then an S election could be made on January 1 following the year of the sale. If the company was always an S corporation and the shareholders revoked Subchapter S status to allow for a Section 1042 rollover at the end of any month other than December 31, then it will become a C corporation. Its termination year would consist of two separate tax years (an S short year and a C short year). Items of income, gain, loss, deduction and credit will need to be allocated between the short years in one of the manners permitted. A revocation would result in a final S corporation return from the beginning of the day preceding the day of the sale (e.g., January 1 through June 30 for a termination effective on July 1), and a C corporation return from the date of revocation through the end of the year (e.g., from July 1 through December 31 for a July 1 revocation date). In either scenario, filing requirements can be managed properly by an experienced tax compliance team and should not be a deciding factor when choosing to sell a business in a certain month.



ARE THERE DISADVANTAGES OF CLOSING AN ESOP SALE AROUND DECEMBER 31?

The popularity of ESOP closings around December 31 can in fact be a disadvantage to closing a transaction at that time. For these types of deals, having a service provider's full attention and capacity can prove to be instrumental in completing a smooth transition. Service providers are likely to be overburdened at the end of the year, especially legal teams, and like many people during the holidays, professionals may be traveling and/or hosting family and friends and the service team may not have as much capacity as usual. As such, service providers may charge more for year-end transactions because they know schedules will be busy. There are also many instances where transactions are unnecessarily rushed in order to close before year-end, when a closing date in the first quarter would make just as much sense. When pursuing an ESOP transaction, as with any other sale or exchange transaction, providing enough lead time is critically important to avoid potentially costly errors.

WHAT ARE SOME ADVANTAGES TO CLOSING AN ESOP SALE AFTER YEAR-END?

Businesses can take advantage of a full year, deductible ESOP contribution no matter what the actual closing date is. For example, if a company closes a transaction on December 31, 2021, it may still have the option to establish the employee stock ownership retirement plan with an effective date of January 1, 2021. This would allow the company to use a full year's worth of eligible payroll to accrue a tax-deductible contribution in 2021, decreasing 2021 taxable income.

Further, the **Setting Every Community Up for Retirement Enhancement Act of 2019**, or SECURE Act, passed in December 2019 provided even more flexibility for companies looking to preserve their eligibility to take a tax deduction for the current year by amending IRC Section 401(b)(2) to allow an employer that adopts a stock bonus, pension, profit-sharing or annuity plan after the close of a taxable year but before the tax return is due (including extensions) to elect to treat the plan as having been adopted as of the last day of the taxable year. This change should further alleviate the rush to adopt plan documents by calendar or fiscal year-end by permitting employers to close a transaction after year-end and still take a tax deduction for the previous year.

While the year-end close can seem attractive to business owners, the importance of completing the transaction by December 31 is often overstated, and transactions can become more expensive and rushed to close "on time." The benefits of an ESOP transaction can be taken advantage of any time of the year, without the rush to meet an arbitrary deadline.

Learn what characteristics make a company a good candidate for a successful ESOP structure.

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