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# Labor Department Draws Line on Worker Classification and Fiduciary Obligations Continue to Grow

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**Labor Department Draws Line on Worker Classification**

The Wage and Hour Division of the U.S. Department of Labor issued Administrator's Interpretation NO. 2015-1 clarifying its position on the misclassification of workers as independent contractors instead of employees. While this sounds like an employment issue, it is an employment issue that has also been arising in the labor context (The NLRB requested comments on its consideration of changing its position to permit independent contractors or staffing employees to organize with part time employees of an employer in a single collective bargaining unit and is considering challenges on joint employer status) which indicates it is part of a larger priority or focus. Reclassification of persons previously not treated as employees will have ripple effects in every benefit plan or program offered.

Employers should consider reviewing the status of individuals classified as independent contractors to verify the classification, and review the employer's policies on retaining such services, related income tax reporting policies, the supporting documentation and operation of the service providers and how these support the employer's position. The best offense is a good defense, at least that's what they say in some sports…

If individuals are reclassified as employees, then an employer may suddenly find it subject to requirements which it previously thought it was exempt from (e.g., moving from under 50 full-time employees or full-time equivalent employees to being subject to the employer shared responsibility penalty or moving out of other small employer exemptions such as under the Mental Health Parity and Addiction Equity Act or moving the employer out of a safe harbor for offering coverage to 70% of full-time employees in 2015 or 95% in 2016 and triggering the employer shared responsibility tax for failing to offer coverage). Employers may find they have an obligation to pay back premiums on the reclassified individuals under insurance policies covering all employees in this group or pay benefits they would have been entitled to receive (e.g., group term life insurance). Employers should consider developing a list of potential, plans, programs, policies (e.g., leave policies) that may be impacted by a reclassification to appreciate the full set of potential risks.

Failing to enroll the individuals prior to reclassification in a 401(k) plan could result in having a group of new employees that should have been enrolled in a 401(k) Plan that was a safe harbor plan, not enrolled, and not receiving safe harbor contributions and the plan losing its safe harbor status and being required to test for nondiscrimination in contributions. There are corrections under EPCRS for employees erroneously excluded from a plan that will also need to be considered as ways to remedy failing to offer a reclassified individual the opportunity to contribute to a 401(k) plan. Employers should carefully monitor the initiative regarding reclassification because it may change many benefit and HR obligations of an employer and an employer's liabilities for providing benefits that were not previously offered.

**Fiduciary Obligations Continue to Grow**

In May, the U.S. Supreme Court clarified in Tibble v. Edision Int'l, Inc. that a retirement plan fiduciary has not only a duty to prudently select investments offered under a retirement plan, but also has a duty to monitor the prudence of those investments and a duty to remove an investment when it is imprudent and that any claim for a breach of fiduciary duty can be brought based on a violation of any of those duties. Employers with defined contribution retirement plans permitting participant directed investments should review how their plan's fiduciary's records or committee minutes document their fulfillment of each of the fiduciary duties clarified under Tibble. A number of cases related to the fiduciary obligations related to participant directed investments as well as employer stock funds continue to work through the courts, so we will likely see additional legal developments in the obligations of fiduciaries. It is never too soon to review your plan fiduciary's documentation of their processes, policies and actions demonstrating fulfillment of their fiduciary duties.

**U.S. Department of Labor Interpretations**

While the U.S. Supreme Court opinion is clearly a statement of the law, we also have additional interpretations coming from the U.S. Department of Labor regarding how they interpret fiduciary obligations from their perspective, however, none of those recent interpretations came in the form of final regulations that had been vetted through the notice, comment and hearing process for moving a regulation into legally binding guidance. Most recently the Department of Labor issued a Field Assistance Bulletin ("FAB") announcing its perspective on what fiduciary duties attach when a plan sponsor offers an annuity as an option in place of a benefit under a defined contribution plan. A plan fiduciary must, under this FAB, monitor the prudence of the annuity contract and provider at the time the annuity is offered to the plan participants and as long as that annuity provider continues to be an alternative for participants to choose. This is similar to the duty to monitor the prudence of the investment option considered in Tibble which requires ongoing monitoring of the prudence of the investment options, with an annuity contract being offered on an ongoing basis, as a form of an investment option, the extension of the duty to monitor the provider on an ongoing basis is not a surprise considering the US. Supreme Court's decision in Tibble.

This is part of the joint efforts by the Treasury Department and the U.S. Department of Labor to facilitate the offering of qualified longevity annuity contracts to participants in defined contribution plans. We will have to wait and see if this FAB provides sufficient incentive for employers to amend their defined contribution plans to provide for the Qualified Longevity Annuity Contracts. The FAB clarifies that an action based on a breach of fiduciary duty under ERISA related to an annuity contract purchased under a defined contribution plan must be commenced within either six years of the last date the fiduciary could have cured the violation or after the last action that was a breach, of within three years of the earliest date the participant had knowledge of the breach. The FAB states that if an action is based on imprudent selection of the annuity provider, the action must be brought within six years of the date on which plan assets were expended to purchase the contract (it is not six years from the date that annuity provider was selected to be an annuity provider for the plan), thus it considers the duty to monitor under Tibble to establish the ongoing duty to monitor the prudence of offering of each annuity provider's contracts under the plan.

Plan fiduciaries offering annuity options or the Qualified Longevity Annuity Contracts as an investment option under their defined contribution plans need to monitor the prudence of the annuity provider's contracts on a regular basis in the same manner as they monitor the prudence of various investment alternatives. Such reviews should be documented by the plan fiduciaries.

**Miscellaneous IRS Guidance on Pension Plan De-Risking and Proposed Change to Equity Compensation Tax Election Procedure**

If you have a defined benefit plan and had been considering de-risking and paying out lump sum benefits to cash out the plan's obligations to pay a life annuity, the IRS recently issued guidance limiting the participants whose benefits can be subject to this de-risking technique particularly with respect to accounts that are currently in pay status.

Equity compensation frequently involves a tax election under section 83(b) to elect to treat as taxable income the amount that was substantially not vested when the property (equity compensation right) was transferred. This election taxes the nonvested portion of an equity grant as taxable at the date of the grant by filing an election with the IRS. The election must currently be filed on paper within 30 days of the grant/transfer and on the individual's federal income tax return. The IRS is proposing to change this because it was concerned that this rule forced individuals to file their returns using paper instead of electronically. Individuals would still be required to file their election with the IRS within 30 days of the date the property was transferred (equity compensation granted). Only the requirement to file the election again with the individual's tax return is eliminated in the proposed change.

While this is only a proposed change, The IRS has stated that it is proposed to apply to transfers of property on or after January 1, 2016 and that taxpayers may rely on this simplified method of electing section 83(b) treatment for property transferred on or after January 1, 2015. This means this simplified method of electing section 83(b) treatment could be used by a taxpayer to file his or her federal income tax return for 2015 in 2016 electronically as long as the election statement is filed within 30 days of the transfer of the property. Individuals should consult their individual tax advisers when preparing their income tax returns and filing any interim elections. This does not change any state income tax requirements related to such equity compensation grants.