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New Compensation And Benefits Rules Demand Early Action

By **Jessica Stricklin, JoAnn Szucs and Lauren Salas Mationg**
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After several years of stability in the compensation and benefits legal landscape, 2023 will bring a series of legislative and regulatory changes that employers will need to address.

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While none of these changes are surprising at this stage, and have been discussed in many articles and blogs, this article provides a high-level overview of the key changes and provides analysis on what employers can expect and how employers should consider addressing the series of changes.

The article is organized into sections on executive compensation, retirement plans and health and welfare plans.

JoAnn Szucs

Executive Compensation

Pay-Versus-Performance Proxy Disclosure

In August 2022, the U.S. Securities and Exchange Commission adopted the long-awaited pay-versus-performance rules under the Dodd-Frank Act that require additional proxy disclosure on the relationship between executive compensation decisions and financial performance.

For calendar year-end companies, the new disclosure must be included in proxy statements beginning in the 2023 proxy season.

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The new pay-versus-performance disclosure consists of three parts: (1) the pay-versus-performance table, (2) tabular list of three to seven of the issuer's most important financial performance measures for linking compensation actually paid to performance in the most recently completed fiscal year, and (3) a clear description of the relationship between compensation actually paid and the financial metrics in the pay-versus-performance table.

Employer Considerations

Aspects of the new disclosure will be time-intensive and burdensome for employers to prepare and will

require input from multiple internal and external advisers. In particular, the fair value calculations of equity awards needed to determine compensation actually paid will require numerous new valuations of outstanding equity awards and may require third-party support to prepare.

Preparation of the disclosure should be well underway to ensure there is enough time to coordinate required inputs and have internal and external review of the new disclosure, including compensation committee review.

At this stage of the process, we are seeing many employers adopt a "less is more" approach to the new disclosure process and tailoring the disclosure to solely the legally required information.

Clawback Policy Changes

In October 2022, the SEC adopted a final rule under the Dodd-Frank regarding the clawback of erroneously awarded incentive-based compensation received by current or former public company executive officers.

Under the final rule, national securities exchanges must adopt listing standards that require issuers to adopt and comply with a written clawback policy. Such policy must provide for the mandatory recovery of any incentive-based compensation awarded to executive officers as a result of erroneously reported financial information received by such individuals in the three-year period preceding the date the issuer is required to prepare the accounting restatement, with limited exceptions.

In addition, the final rule requires issuers to comply with certain reporting and disclosure requirements related to the clawback policy including (1) filing the policy as an exhibit to the issuer's annual report, (2) reporting checkboxes on the issuer's annual report to indicate if the financial statements reflect the correction of an error to previously issued financial statements and whether such correction requires recovery analysis under the clawback policy and (3) disclosing certain actions taken pursuant to the issuer's clawback policy.

The final rule was published on the Federal Register on Nov. 28, 2022, which starts the clock for national securities exchanges to propose and adopt clawback listing standards.

Employer Considerations

Public company employers will likely be required to be in compliance with new listing standards by late 2023 or early 2024.

Accordingly, public company employers that will be subject to the new clawback rules should begin reviewing their existing policies to consider what changes may be required and begin planning for the new or revised clawback policy adoption and implementation, including considering determination procedures for executive officers and potential changes to the structure of current executive compensation programs.

Foreign private issuers and multinational companies should also consider potential compliance complexities that may exist due to local law requirements.

We also anticipate that the new rules will require considerable employee communications, given the breadth of the new rules. Employers subject to the new rules should begin internal discussions on

communication strategy now.

Amended Rule 10b5-1 Plan Rules

In December 2022, the SEC adopted final amendments to the rules regarding Rule 10b5-1 plans and disclosure requirements.

Under the final rules, officers and directors entering into Rule 10b5-1 plans after the rules are effective are subject to new rules and restrictions, including required certifications, 90-day cooling-off periods before trading can commence and restrictions on overlapping plans and single trade limits. Additionally, public company employers are subject to the following disclosure requirements, effective for periodic filings and Forms 4 and 5 filed on and after April 1:

Quarterly Disclosures

Disclosure of the material terms of Rule 10b5-1 plans entered into by directors and officers during the prior fiscal quarter in periodic reports, excluding pricing terms.

Annual Disclosures

- Disclosure in an issuer's Form 10-K and proxy on whether an insider trading policy and procedures have been adopted — and if not, why — and filing of any such adopted policies as an exhibit to Forms 10-K and 20-F.

- Narrative disclosure in an issuer's proxy on the issuer's option grant policies and practices regarding stock option and stock appreciation right grants.

- Tabular disclosure in the issuer's proxy statement of stock option grants made to a named executive officer four business days before and/or one business day after the filing for Forms 10-Q, 10-K or 8-K that discloses material nonpublic information, including earnings releases, but excluding a Form 8-K that discloses only a material new option award grant.

Section 16 Reports

- Checkbox reporting on Forms 4 and 5 to report that reported transaction is intended to satisfy the affirmative defense conditions of Rule 10b5-1.

- Disclosure of bona fide gifts made by the Section 16 filers on Form 4, instead of Form 5, within two business days of execution of the transaction.

Employer Considerations

Public company employers should begin educating directors and officers about the final Rule 10b5-1 plan rules and ensure that any policies and procedures on Rule 10b5-1 plans are consistent with the amended rules.

Although Form 10-K and proxy disclosure requirements will not be required until such forms are filed in early 2025 for calendar year-end companies, public company employers should also begin considering potential amendments to insider trading policies and grant practice policies, including the current

provisions on trading windows and the treatment of gifts.

In particular, public company employers may want to avoid narrative and tabular disclosure of option grants in the proxy under the amended rules by ensuring the grants are made in an open trading window that is more than four business days before or one business day after the release of material nonpublic information.

Retirement Plans

SECURE 2.0 Act of 2022

The SECURE 2.0 Act of 2022 was signed into law in the final days of 2022. The act contains several provisions affecting qualified retirement plans.

In particular, the act:

- Requires automatic enrollment in certain new 401(k) and 403(b) plans;
- Clarifies named fiduciary rules with respect to pooled employer plans;
- Expands participation in multiple employer plans and pooled employer plans to include 403(b) plans;
- Further increases the required minimum distribution age for mandatory distributions from age 72, as implemented under the SECURE Act of 2019, to age 73 beginning Jan. 1, 2023, and to age 75 beginning Jan. 1, 2033;
- Applies a higher catch-up contribution limit for employees who have attained ages 60, 61, 62 and 63, which will be subject to adjustment for inflation after 2025;
- Allows employees to receive employer matching contributions based on their repayment of student loans under 401(k), 403(b), and certain governmental plans;
- Includes an exception for certain emergency expense distributions and qualified birth or adoption distributions from the 10% tax that generally applies to early distributions from qualified retirement plan accounts;
- Expands the automatic cash-out features under qualified retirement plans to assist with the rollover of amounts to eligible retirement plans;
- Further improves coverage for long-term part-time workers in 401(k) and 403(b) plans by requiring eligibility after either 1 year of service with 1,000 hours of service or 2 years of service with 500 hours of service, decreased from 3 years of service with 500 hours of service under the SECURE Act of 2019;
- Includes guidance on life annuities and qualifying longevity annuity contracts;

- Provides correction guidance on overpayments, excise taxes for late required minimum distributions, missing participant programs, automatic enrollment deferral failures and the expansion of the Employee Plans Compliance Resolution System;

- Requires updates to the disclosure and content of certain retirement plan notices; and

- Includes the ability to treat employer matching or nonelective contributions as Roth contributions.

Employer Considerations

Now that the act is finally law, employers should determine the appropriate timing for the act's mandatory provisions and consider which optional provisions are beneficial and should be implemented.

DOL Final Amendment to ESG Rules

The U.S. Department of Labor issued a final amendment to the environmental, social and governance rules in November 2022. The amendment takes a different view on ESG investments than the 2020 rules that were issued under the Trump administration, relaxing the requirements for the selection of ESG investments under qualified retirement plans. The amendment also contains provisions on proxy voting.

Employer Considerations

As ESG continues to gain more and more attention, both positive and negative, retirement plan fiduciaries should consider whether ESG concerns should now factor in selecting plan investments. While the rules have been relaxed, plan fiduciaries remain subject to the general Employee Retirement Income Security Act standard of operating solely in the interests of plan participants and not broader concerns. ESG investments should be reviewed carefully before implementing.

DOL Proposes Changes to VFCP

In November 2022, the DOL proposed the first substantial changes to its Voluntary Fiduciary Correction Program in several years. The restated VFCP and proposed amendment to the prohibited transaction class exemption 2002-51 provide clarity and some flexibility related to the correction of late employee contributions, party-in-interest transactions and investigations. Comments on the changes are due by Jan. 20.

Health and Welfare Plans

Telehealth Relief

Under the Coronavirus Aid, Relief and Economic Security Act, and a subsequent extension by the 2022 Consolidated Appropriations Act, participants were no longer required to satisfy a minimum deductible when using telehealth services.

The legislation also affirmed that these services would not adversely affect a high deductible health plan participant's health savings account eligibility. The relief was set to expire Dec. 31, 2022, but was recently extended through Dec. 31, 2024.

Accordingly, high deductible health plan participants can continue to benefit from predeductible coverage for telehealth services and continued health savings account eligibility for at least the 2023 and 2024 plan years, assuming the employer's health plan year is a calendar year.

Employer Considerations

Employers should communicate the extended relief period to employees and that ensure insurers and third-party administrators are accurately applying the deductible relief for telehealth services.

Form 1095 Furnishing Extensions

The Affordable Care Act requires employers to provide a Form 1095-B or 1095-C to individuals by Jan. 31 following the calendar year in which the coverage was provided. Initial relief extended the due date until 30 days following Jan. 31, or the next business day if Jan. 31 is not a business day.

Under new relief, the deadline is extended to March 2 of each year, or the next business day if March 2 falls on a weekend or holiday.

For the 2022 forms, which are due in 2023, the furnishing deadline is March 2, 2023. Note that this relief only adjusts when the 1095 forms must be furnished to individuals and not when the forms, including Form 1094, must be filed with the Internal Revenue Service.

Employer Considerations

Employers who rely on their insurer or a third-party vendor to distribute Forms 1095 confirm the insurer's/vendor's distribution timeline continues to comply with the required deadline or the applicable relief.

Conclusion

Given the extent of changes that will become effective in 2023 or require work in 2023, employers should work early in 2023 to allocate responsibility and resources for the changes. Unlike many recent years, the extent of the changes will require work and analysis early in 2023 and cannot wait until the fourth quarter, as is often the case.

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