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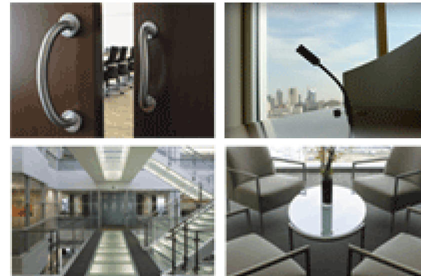

HEART Support for Our Troops Will Affect Employee Benefit Plans

by Charles. M. Cain II and Gordon Earle Nichols

Earlier this spring, Congress passed the Heroes Earnings Assistance and Relief Tax Act of 2008 (the "Act"), commonly referred to as the HEART Act, which was signed into law by President Bush on June 17, 2008. The Act addresses several different operational issues arising under private sector benefit plans in which employees called into active duty participate. All employers should review these new rules and consider the impact on their employee benefit plans.

Differential Wage Payments

Generally, a "differential wage payment" is compensation paid by an employer that represents all or a portion of the wages the employee called into active duty would have received from the employer if the employee was, instead being in active duty, performing services for the employer, regardless of the employee's legal right to any portion of such payment. For differential wage payments made *after* December 31, 2008, the Act provides that such payments made to individuals who are on active military duty for more than 30 days are subject to income tax withholding. In addition, if an employer makes differential wage payments, they must be treated as "Compensation" under an employer's qualified retirement plan. As a result, differential wage payments must be taken into account for purposes of elective deferrals and employer contributions to any tax-qualified retirement plan.

- Action Item: Payroll systems will need to withhold from differential wage payments made to employees in active duty made for more than 30 days. The definition of "Compensation" in most tax-qualified retirement plans will likely need to be amended to include differential pay. Although amendments are not required until the last day of the first plan year beginning on or after January 1, 2010, it is advisable for administrative purposes to have the language in the plan by the beginning of next year.

Benefit Accruals

The Uniformed Services Employment and Reemployment Rights Act ("USERRA") provides that tax-qualified plans **must** recognize qualified military service of those employees who return to work after completing such service for vesting and benefit accrual purposes. Under USERRA, employees returning from qualified military service **may** make catch-up contributions to a tax-qualified retirement plan (up to the amount the individual could have made if the individual had remained employed) within a period equal to the lesser of (i) three times the length of the qualified military service or (ii) five (5) years. If an employee makes such contributions, the employee is entitled to accrued benefits that are contingent on employee contributions (e.g., employer matching contributions).

However, under the Act, qualified plans also **may** (but are not required to) recognize qualified military service for benefit accrual purposes for employees who do not return to employment with the plan sponsor due to death or disability. If a plan provides such crediting, it must do so on a reasonably equivalent basis for all employees who die or become disabled while performing qualified military service. For the purpose

the Pension Protection Act of 2006 for employees called into active military service for a period of at least 180 days or for an indefinite period.

- Action Item: Although most tax-qualified retirement plans already include distribution provisions for a severance from employment, they will likely need to be amended to include the six-month suspension period following distributions related to qualified military service.

If you have any questions about the HEART Act, please contact one of the Employee Benefits and Executive Compensation attorneys at Boult, Cummings, Conners & Berry PLC:

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