

Compliance Directions

Balancing Cost-Saving Strategies with Employee Benefit Obligations Amid Economic Uncertainty **Gallagher**

Economic uncertainty may cause some employers to face reducing employee hours or layoffs to cut costs. When downsizing, employers must carefully consider the impact on health and welfare benefits. It's crucial to avoid errors that could have significant implications for both employees and employers. This article explores issues related to workforce reductions and highlights some key employee benefit considerations.

Eligibility Considerations

Facing economic challenges, many employers might consider limiting employees' hours below the ACA full-time threshold of 130 hours per month to reduce the number of employees classified as full-time, thereby minimizing the need to offer coverage and avoiding Employer Mandate penalties. However, Section 510 of ERISA prohibits employers from actions that interfere with an employee's rights under a benefit plan, including reducing hours to prevent eligibility for health coverage. Employees have filed lawsuits claiming that reductions in hours constitute discrimination and interfere with their access to health benefits, often citing evidence of employers' intent to cut healthcare costs. While employers have discretion over work hours, those subject to ERISA should carefully communicate the reasons for reducing hours. Employers using the ACA Look Back Method must be cautious when discontinuing coverage for employees who fall below full-time status, as their status may be protected based on the method used to determine ACA full-time status.

Furloughed Employees

When an employer furloughs an employee, the employment relationship remains, but this does not automatically ensure continued eligibility for health and welfare coverage. Employers must review their plan documents and insurance policies to confirm eligibility criteria, often defined by hours worked or ACA guidelines. If coverage is continued for furloughed employees without insurer agreement, the employer risks self-insuring those employees. Employers should consult with insurers or stop loss carriers to secure agreement for continued coverage during furloughs, as insurers may allow coverage to continue for a few months if the policy includes necessary provisions. Employers must review and possibly amend their policies to reflect the desired coverage terms. If no

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amendments are made and coverage ends, COBRA or conversion rights should be offered. Generally, employees can be reinstated to their plans upon returning from furlough.

Employee Cafeteria Election Changes

Employers who design plan eligibility based on ACA counting hours requirements may face restrictions on when employees can change their benefit elections. A furlough does not alter an employee's full-time status, so they remain eligible for the plan and cannot drop coverage. Although reduced hours might make coverage less affordable, it does not create an opportunity for a change in benefit elections. However, IRS rules allow a midyear election change for employees whose hours drop below 30 per week, enabling them to drop coverage if they plan to enroll in other minimum essential coverage immediately. To facilitate this, the employer's cafeteria plan must incorporate the IRS-permitted event.

Employee Payment Issues

When employees face a pay shortage due to furloughs or reduced hours, they may lose the ability to make pre-tax contributions toward their benefits. Employers can cover the employee's premium portion but should consult a tax advisor about potential implications. If covering the premium is not feasible, other options are available.

Although the IRS hasn't provided specific guidance for non-FMLA situations, it has outlined options for paying benefits during unpaid FMLA leave: (1) prepayment via special salary reduction, (2) pay-as-you-go on an after-tax basis, or (3) catch-up salary reductions upon return. It is likely that these options would also be available in a non-FMLA context.

Plans (and plan documents) should be flexible to accommodate these methods. If a pay shortage covers only some salary reduction elections, employers must decide the order of reductions. Plan sponsors should establish a uniform practice, possibly prioritizing health, disability, and life insurance benefits, and ensure cafeteria plan documents reflect this order, with policies communicated to employees.

COBRA Considerations

Continuation coverage under COBRA must be offered to qualified beneficiaries, such as employees, retirees, and dependents who lose coverage due to qualifying events like termination or reduced work hours. Plan sponsors and administrators are required to provide COBRA election notices, detailing rights and procedures, within specific

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timeframes: 14 days after receiving notice of a qualifying event, or 44 days if the employer is also the plan administrator. Failure to provide timely notices can lead to lawsuits and fines, especially during large-scale layoffs. Employers must ensure compliance, despite challenges with dispersed workforces, to avoid penalties under the Internal Revenue Code and ERISA, as well as potential class action lawsuits. Employers with fewer than 20 employees should check state continuation rules and coordinate with insurers to ensure coverage for those losing benefits.

Plan Documents

When employers decide to furlough employees or implement layoffs, they must review their plan documents to assess the impact on benefits and consult with insurers, TPAs, and stop loss insurers to avoid compliance issues. ERISA employers must adhere to fiduciary rules, administering plans as written to avoid breaches and unintended self-insurance of claims. Any plan changes, such as extending eligibility for furloughed employees, require amendments and communication to participants. Employers must provide updated summary plan descriptions or summaries of material modifications within required timeframes. Stop loss insurers rely on plan documents or SPDs for payment administration, so they must receive updated documents reflecting any changes.

Conclusion

Navigating the complexities of workforce management during economic challenges, employers must carefully balance cost-savings with compliance obligations under the ACA, ERISA, COBRA and other federal laws. Employers facing the possibility of a reduction in force should thoroughly review and amend plan documents as necessary and consult with insurers and TPAs to mitigate compliance and financial risks. For a deep dive into these issues and more, check out our Spotlight, [Reduction in Hours, Furloughs and Layoffs and the Impact on Employee Benefits](#).

The intent of this article is to provide general information on employee benefit issues. It should not be construed as legal advice and, as with any interpretation of law, plan sponsors should seek proper legal advice for application of these rules to their plans.