



Ivins Phillips Barker

CHARTERED

Are Your Benefit Plans Keeping Pace with the New Reality?

August 12, 2020

Furloughs. Reduced hours. Temporary leave. The global pandemic has added complexity to existing leave rules, as employers adjust their workforces to address the pandemic and new and changing economic realities. As a result, the once relatively straightforward question of an employee's "employment status" – and the employee benefits implications that correspond with that status – has grown ever more complex.

This alert highlights the issues that often arise when these new workforce policies and strategies are not carefully integrated with the terms of employee benefit plans, including:

Four Common Issues for Retirement & Savings Plans

- Inconsistency between the definition of "disability" under the LTD and pension plans
- Failure to properly credit the leave or furlough period under the plan
- Failure to count non-wage pay as "eligible compensation" under the plan
- Failure to accurately identify whether a "termination of employment" has occurred

Three Common Issues for Health & Welfare Plans

- Failure to terminate coverage during the period of absence in contravention of Plan terms
- Failure to collect employee premium contributions
- Failure to meet the notice requirements of COBRA

Overview

Amid the fast evolving economic and regulatory landscape of the COVID-19 pandemic, it is understandable that we find ourselves in this place. New forms of leave have been launched quickly, in response to the CARES Act and to address rapidly developing workforce challenges, without giving full consideration to benefit plan implications. In addition, leave programs may have been coordinated with the specific provisions and terminology of existing benefit plans when established, but over time, these leave policies often drift slowly out of sync. This can be further exacerbated where leave administration is outsourced to a third party with no responsibility for benefit plan administration, compounded by an unfamiliarity with specific plan terms. Specifically, long-term disability (LTD) programs and traditional extended leave policies have long presented opportunities for confusion or inconsistency among the provisions of various welfare and pension plans.

Complicating matters further, the global pandemic has caused employers to embrace furloughs and short-term layoffs to temporarily adjust their workforces to meet evolving challenges. By their very nature, these policies are implemented quickly, with an eye focused squarely on critical employee relations and financial considerations. Even where thoughtfully designed, these temporary programs are often adopted without a thorough review of how they align with the actual language of the remaining plans.

Taken altogether, this lack of coordination and consistency can result in ambiguity and confusion as to a participant's entitlement under the plans, or an outright failure to follow the terms of an ERISA plan – resulting in risk to participants, plans and sponsoring employers.

Four Common Issues for Retirement & Savings Plans

Four issues typically arise with respect to pension and savings plans:

- **Inconsistency between the definition of “disability” under the LTD and pension plans**

Inconsistency in the definitions among plans can lead to confusion, compliance failures and unintended results. In addition, when the DOL issued new claims regulations for disability benefits in 2018, many companies switched to using the Social Security Disability Insurance (SSDI) standard in their pension plans to define disability (in order to avoid the more stringent new rules). This may differ from the standard used by LTD carriers or under an LTD plan. As a result, participants who qualify for LTD benefits may be dismayed to learn that they are not eligible for a disability pension – or vice versa.

- **Failure to properly credit a leave or furlough period under the plan**

- Various types of leave, furlough or other absence may not be clearly addressed under pension plan terms that define “service.” This can have unfortunate implications for plan eligibility, vesting, and early retirement. Even where clearly defined, these leave programs are often communicated to employees (by the employer or the carrier) in a manner inconsistent with those plan terms.
- For example, the service counting rules promulgated by the Department of Labor and Treasury require that, in most cases, employees be credited for periods in which no duties are performed due to leave of absence. These rules are frequently overlooked.

- **Failure to count non-wage pay as “eligible compensation” under the plan**

- For periods of paid leave or LTD, it is often unclear how the compensation will be treated under other benefit plans. For example, can 401(k) deferrals be deducted from this pay? Does it count as pensionable pay under a final average pay pension formula? The design of the leave or furlough policy may have assumed a treatment of compensation under the qualified plan that may not align with the actual plan terms. Even if there is no inconsistency, the payroll codes may need to be updated to appropriately capture or exclude compensation) related to the leave period. This can be complicated in the case of LTD income, which may be paid by a third-party insurance company outside the payroll system. In addition, LTD benefits can be pre-tax or post-tax depending upon the plan design and taxation of premiums.

- **Failure to accurately identify whether a “termination of employment” has occurred**

- Ambiguity regarding an employee's status as “active” or “terminated” – or something in between – can create confusion and a host of compliance issues. If the employer treats an extended leave or furlough as a termination of employment, it triggers the following significant consequences for the qualified plans:

- Enabling a full distribution from the 401(k) plan and possible commencement of pension benefit
 - Requiring a participant over age 72 to start required minimum distributions (RMDs)
 - Negatively impacting eligibility for retiree medical benefits (if limited to active retirees) or eligibility for subsidized early retirement (if limited to active retirees)
 - Triggering accelerated repayment of an outstanding loan from a 401(k) plan (or default)
- There are numerous implications outside of a qualified plan including recall or rehire rights, implications regarding deferred compensation payments governed by Code Section 409A, and loss of eligibility for active health care coverage (discussed below).

Three Common Issues for Health & Welfare Plans

Leave of absence, short -layoff, or furlough policies often expressly provide for either the continuation or termination of medical coverage during the term of the leave. Employers often knowingly choose to extend benefit coverage for some or all of these periods of absence, as a means of cushioning the impact of a layoff. This subsidized continuation coverage may be promised in writing as part of the layoff or voluntary retirement materials. Unfortunately, where that communication deviates from health insurance contracts or plan documents, the employer's design intent can be frustrated. Three typical compliance issues arise for health and welfare plans:

- **Failure to terminate coverage during the period of absence in contravention of Plan terms**
 - *Health Plan.* Although an employer may promise continued medical coverage during periods of leave of absence or furlough, this may not necessarily be supported by the underlying plan document or insurance contract. Frequently, these documents condition eligibility on a threshold number of hours worked (or regularly scheduled), and a classification status such as "full-time," "regular," or "active." Violating the eligibility terms of an insured plan will result in a denial of medical claims by the carrier. For a self-insured plan, the consequences of violating the eligibility rules could be exposed during a plan audit.
 - *Welfare Plans.* Similar issues arise under other insured welfare plan arrangements. If the eligibility terms are not followed, a life insurance carrier will deny claims if the participant should pass away during the term of the absence. Similarly, a stop-loss carrier will deny employer claims for expenses incurred during the period of unauthorized coverage.
- **Failure to collect employee premium contributions**
 - Welfare plan participation generally requires an employee's continued payment of the employee's premium contribution. Complications can arise during periods without pay, or in which employees are receiving benefits such as STD/LTD from third parties. Typically, employers develop "workarounds" to deal with these situations – often suspending or deferring the contributions – without reflecting those provisions in the language of the plan, leading to the eligibility issues described above.
- **Failure to meet the notice requirements of COBRA**
 - COBRA obligations are triggered by a loss of coverage. Lack of precision regarding the termination of a participant's benefits can lead to COBRA notice failures. This can be exacerbated when COBRA administration is outsourced to a third party that may not have modified its processes to reflect new forms of employment status and the impact on benefit eligibility.

Conclusion

The issues highlighted above can be addressed by conducting a thoughtful review of applicable plan language and contracts in light of the new forms of leave or other programs that the employer has established (or is considering establishing). A fresh review of that plan language will also help employers develop clear and consistent terminology to be used in communicating these policies and programs to employees, eliminating potential confusion and risk, including the risks highlighted above. As always, this necessary housekeeping is more easily addressed now, before conflicts or live issues arise.

For questions, please contact a member of our [Benefits Team](#). For more information on benefits issues related to the pandemic, please visit our [COVID-19 Resources Page](#).