Bodman PLC | COVID-19 Response Team Website **April 2020**

Continuing Group Health and Welfare Benefits for Employees on Furlough or Layoff

In response to the COVID-19 crisis, many employers have been forced to furlough or lay off employees. At the same time, many employers have expressed a desire to continue group health and welfare benefits for the employees whose hours are being reduced due to a lack of work, or who are being furloughed or laid off on a permanent or temporary basis. There are a number of issues that an employer in this situation should consider when evaluating whether to continue to provide group health and welfare benefits to those employees facing a reduction of hours, layoff or furlough. The following summarizes those considerations.

Eligibility. Eligibility for group health and welfare benefits is determined by the applicable plan terms. The plan provisions frequently condition eligibility on employment status. For example, the individual must be within the class eligible to participate in the arrangement (e.g., must be an employee) and work a specified number of hours in the applicable measuring period (e.g., 30 hours per week). If an employee is "permanently laid off" and that means a termination of employment with no expectation of being re-employed, the permanently laid-off employee may no longer be eligible to participate in the plan (i.e., no longer in an eligible class and not working sufficient hours). If an employee's hours are reduced, they continue to be employed but are no longer eligible for the benefit due to a failure to complete sufficient hours to remain eligible for the benefit. If an employee is placed on "furlough" or "temporary layoff" and that means that an employee is in unpaid, non active status where no duties are performed, with an expectation that the employee will return to employment at some future date, the individual may continue to be considered an "employee" for employment purposes but the employee may no longer be eligible under the plan (i.e., insufficient hours of service to satisfy the eligibility threshold). Plans may have provisions which address furlough or temporary layoff. Alternatively, plans may have "approved leave" or "leave of absence" provisions which would allow a furloughed or temporarily laid-off employee who is still in an eligible class (i.e., treated as employed) but who lacks sufficient hours, to continue to participate in the plan for some period of time. Plans that have no such provisions, could be amended to include such a provision.

Comment: It is critical that the plan and related documents (e.g., summary plan description) and in the case of a fully-insured benefit the underlying insurance contract, or in the case

of a self-insured arrangement, the stop loss policy if there is one, mirror each other as to the benefits provided. Otherwise, the employer may find itself paying for the entire cost of the benefit, if the insurance carrier denies coverage because the policy does not cover employees on furlough or who have been temporarily laid off. In order to mitigate the risk of a carrier denying these types of claims, employers should confirm with their brokers or the carriers that the furloughed or temporarily laid-off employees will continue to be covered under the terms of the insurance policy or stop loss coverage.

Premium Payment. Generally, participants pay for a portion of the premium cost associated with the health and welfare benefits that they receive (cost-sharing). Accordingly, the employer wishing to continue benefits for the furloughed or temporarily laid off employees will have to decide how the participants' cost-sharing will be paid for. The employer could establish a premium holiday for the impacted employees and pay the entire cost associated with the benefit for some period of time. See below regarding discrimination considerations. Alternatively, the plan should have provisions, or could be amended, to allow the impacted employees to prepay, pay as they go on an after-tax basis or reimburse the employer after they return to work for their share of the benefit costs.

Most employees pay for their cost-sharing on a pre-tax basis through Section 125 plans (a/k/a premium conversion plans, flexible benefit plans or cafeteria plans). Elections made under these arrangements must generally be irrevocable for the entire plan year, but the plan may include exceptions to this irrevocability rule and permit midyear election changes. Employers should review their Section 125 plans to ensure that changes can be made to employees' cost sharing.

Comments: In order to implement a premium holiday, it is likely that the applicable plan documents, including summary plan descriptions and possibly the underlying insurance contracts, would have to be amended to accommodate the change. These changes would need to be communicated to the participants.

Nondiscrimination. For purposes of fully-insured group health care arrangements, employers can pay the entire premium cost for the furloughed or temporarily laid-off employees and the premium and the benefits provided will continue to be excluded from the income of the furloughed or temporarily laid off employees. Under the current discrimination rules applicable to fully-insured group health care arrangements, employers could choose to pay monthly premiums for some but not all impacted employees.

The same general rules apply for purposes of self-insured group health care arrangements with a very important caveat. Self-insured plans are subject to discrimination rules that are designed to make sure that highly paid employees do not receive more favorable benefits than non highly paid employees. These nondiscrimination rules could come into play if highly paid employees are among the furloughed or temporarily laid-off group receiving the benefit.

COBRA Continuation Coverage. COBRA rules generally apply if an employer with 20 or more employees sponsors a group health plan. Under COBRA, employers must offer continuation of group health coverage to employees, former employees and their dependents when group health plan coverage is lost due to certain qualifying events, such

as termination of employment or reduction of hours. In the event of a temporary layoff or furlough, the individual may still be considered an employee but group health coverage could nevertheless be lost due to a reduction in hours. The provisions of the plan should be reviewed to determine when an employee would lose coverage due to a reduction in hours (e.g., the number of hours worked in a given time period can be measured based on the preceding month or quarter). The length of the temporary layoff or furlough and the measuring period will impact when an individual loses coverage due to a reduction in hours.

If there is loss of coverage as a result of reduction in hours, a COBRA notice would be required. If hours are reduced and the employer continues the coverage, there would be no loss of coverage and no COBRA notice would be necessary until coverage is actually lost. The employer should confirm with any insurance provider, in the case of a fully-insured group health plan or the stop loss carrier, if any, in the case of a self-insured group health plan, as to how the carrier will treat an extension of coverage when there has been a reduction in hours but the employer desires to continue coverage.

An alternative would be to treat the temporary layoff or furlough as resulting in a loss of coverage due to reduced hours thereby triggering the COBRA notice. The employer could, but is not required to subsidize, in whole or part, the cost of COBRA coverage. Caution should be exercised because if the health plan is self insured and the subsidy is not broadly offered it could run afoul of the nondiscrimination rules described above. If the employer does offer to subsidize all or a portion of the COBRA cost, the employer should clearly communicate to the impacted employees the extent of the subsidy (i.e., employee only vs. spousal or dependent coverage), the duration of the subsidy, and eligibility for the subsidy (e.g., only available if a valid COBRA election is made).

Comment: Many third party administrators will only want to process a temporary layoff or furlough situation as resulting in a reduction of hours and a loss of coverage triggering a COBRA notice. It is very important to coordinate treatment of a temporary layoff or furlough with the appropriate vendors so the employer is not faced with a gap in coverage.

Affordable Care Act (ACA). Under the ACA, an applicable large employer (ALE) with 50 or more full time employees that sponsors a group health plan that does not offer minimum essential coverage to at least 95% of its full time employees (and their dependents), and such coverage does not meet certain affordability and minimum value requirements under the Code, could be subject to a penalty for either a coverage or affordability failure. The coverage and affordability penalties are predicated on any employee purchasing subsidized coverage through an exchange. Temporary layoffs, furloughs and reductions in hours complicate compliance with these rules as well as increasing the likelihood of a reporting error.

For ALEs that have adopted the look-back testing method, if the employee has averaged sufficient hours (e.g., 130 hours per month) during the look-back period (e.g., a 12 month period) their status is fixed as a “full-time employee” for the next stability period (e.g., plan year) regardless of the number of hours actually worked during the stability period. If an employee is considered to be a “full-time employee” whose hours are reduced below 30 per week but more than zero, the group health benefits will have to be continued to avoid the ACA coverage penalty or the ALE would run the risk of a coverage failure penalty if any

employee obtained subsidized exchange coverage. If the actual reduction in hours results in a COBRA event for the employee, and the employee pays the full COBRA coverage rate, this could make coverage unaffordable and might trigger the affordability failure penalty if any employee obtains subsidized coverage on an exchange. In this case, it may be more cost effective to simply continue offering coverage at employee rates.

For ALEs that adopted the monthly testing method, if the employee's hours are reduced to less than 30 hours per week but more than zero, medical benefits would not have to be offered but the reduction would likely trigger a COBRA event due to the loss of coverage due to insufficient hours to remain eligible for the benefit. If hours are reduced but remain 30 hours per week or more but less than the number of hours necessary to remain eligible for coverage, the employer should consider continuing to offer coverage to avoid a potential coverage failure penalty. The alternative would be to risk the penalty if any employee obtains subsidized exchange coverage. If the employer continues coverage but requires the employee to pay the full cost of the coverage or treats the reduction as a COBRA event and the employee pays the full COBRA continuation coverage rate, the cost of coverage would likely be unaffordable, potentially exposing the employer to the affordability penalty if any employee obtains subsidized exchange coverage.

If an employee stops working for the ALE due to temporary layoff or furlough (i.e., hours are reduced to zero) and then returns, it is necessary to determine whether the employee is considered to be 1) a continuing employee, or 2) a terminated and rehired employee. If the returning employee is deemed to be a continuing employee, then the ALE will avoid liability only if the employee is offered coverage as of the first day that the employee is credited with an hour of service or, if later, as soon as administratively practicable (offering coverage by no later than the first day of the calendar month following resumption of services is deemed to be as soon as administratively practicable). If the returning employee is deemed to be a terminated and rehired employee, the ALE can delay the offer of coverage until such employee once again satisfies the plan's eligibility and waiting period rules. An employee will be considered to have terminated employment and be a rehire—and may be treated as a new employee upon return—if the employee has a period of 13 consecutive weeks during which the employee is not credited with an hour of service. Otherwise, the employee would be treated as a continuing employee.

Comment: Given any employer's particular facts and circumstances, the complexity of the rules and the ongoing release of guidance associated with the COVID-19 crisis, employers should consult with their benefit advisors, vendors and benefit counsel and be fully advised before implementing any plan design changes or adopting policies and procedures for continuing health and welfare benefits for employees on temporary leave or furlough.

If you have any questions, please contact your Bodman attorney or Rebecca O'Reilly at (313) 392-1050 or roreilly@bodmanlaw.com or Dave Walters at (248) 743-6052 or dwalters@bodmanlaw.com. Bodman cannot respond to your questions or receive information from you without first clearing potential conflicts with other clients. Thank you for your patience and understanding.