

HR COMPLIANCE OVERVIEW



Employee Compensation and Benefits During Layoffs and Furloughs

During periods of economic or business uncertainty, employers may need to downsize their workforce. Such reductions can take a variety of forms but frequently include employee layoffs or furloughs. Employers who take these measures must ensure that they are in compliance with laws governing compensation and employee benefits. Some key benefits and compensation issues to consider include:

- Health plan coverage;
- Employer shared responsibility rules;
- Right to continue coverage under federal and state coverage continuation laws;
- Payment of wages under the Fair Labor Standards Act (FLSA);
- Payout of accrued but unused paid time off; and
- Unemployment compensation.

This Compliance Overview summarizes the employee benefits and compensation issues employers may encounter when terminating or suspending employment. However, this Compliance Overview only addresses federal requirements. Therefore, employers may also consider reviewing state and local laws for additional legal requirements.

LINKS AND RESOURCES

- U.S. Department of Labor (DOL) unemployment insurance [guidance](#)
- WARN Act [employer guide](#)
- DOL [FAQs](#) on COBRA continuation coverage
- IRS [guidance](#) on the ACA's employer shared responsibility rules

Employee Compensation

- Employees are generally not required to be paid for time spent not working.
- Exceptions apply to exempt employees who work for part of a workweek and employees eligible for paid leave.
- Employers may provide paid leave beyond what is legally required.
- Employees may be eligible for expanded unemployment benefits.

Employee Benefits

- Whether employees remain eligible for health plan coverage depends on the terms of the plan.
- ALEs may need to maintain coverage for furloughed employees to avoid penalties under the ACA's employer shared responsibility rules.
- If active health plan coverage ends, employees who are furloughed or laid off may be eligible for continuation coverage.

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Overview of Layoffs and Furloughs

Furloughs

In some instances, such as a temporary lack of work or a temporarily reduced budget, employers may consider placing employees on furlough. A furlough is typically a temporary unpaid leave of absence or reduction in hours. A furlough differs from an employee layoff in that employees are still considered employees of the employer and usually are provided an approximate date by which they will return to their prior position or full work schedule.

Layoffs

In cases of economic downturn, business closures or similar disruptions, employers may instead choose to lay off employees. Layoffs are different from furloughs because laid-off employees are no longer employees of the employer or on the employer's payroll. Often, employers intend for layoffs to be a temporary separation from employment, leaving open the possibility of the employee returning to work at a later date when business conditions improve. At other times, layoffs are permanent, either because the employer intended for the layoffs to be permanent or because business conditions do not sufficiently improve.

Employee Benefits Considerations

Health Plan Coverage

Employers may continue active health plan coverage for furloughed employees, depending on their health plan's eligibility rules. For example, a health plan may require employees to work a minimum number of hours to be eligible for coverage and include rules for how to account for short-term leaves of absence, whether paid or unpaid. Employers should review the terms of their written plan documentation to determine the eligibility rules that apply to furloughed employees. As explained below, special coverage requirements apply to applicable large employers (ALEs) under the Affordable Care Act's (ACA) employer shared responsibility rules. In general, active health plan coverage for laid-off employees should be terminated, as they are no longer considered employees, although they may be eligible for continuation coverage.

Employers that want to expand eligibility for furloughed employees may have the option of amending their health plan's written terms to do so. However, employers should check with their insurance carriers, including a stop-loss insurance carrier, before expanding their health plan's eligibility rules. Employers that expand coverage outside the terms and conditions of the plan without consent from the insurer may face significant financial exposure.

In addition, during a furlough, employers may choose to pay the employees' share of premiums in full or in part. Employers that pay for employee premiums will need to comply with any applicable cafeteria plan rules and nondiscrimination requirements to ensure favorable tax treatment.

Employer Shared Responsibility Rules

The ACA requires ALEs to offer affordable, minimum-value health coverage to their full-time employees (and dependents) or potentially pay a penalty to the IRS. ALEs are employers that averaged at least 50 full-time employees, including full-time equivalent employees, during the preceding calendar year.

Terminating group health coverage for a full-time employee during a furlough may trigger an employer shared responsibility penalty for an ALE if the employee is still considered to be employed by the employer. This is more likely to be an issue for ALEs that use the look-back measurement method to determine full-time employee status. Under the look-back measurement method, individuals determined to be full-time employees for a stability period must generally be offered coverage for the entire stability period as long as they remain employed. Upon layoff, an employee is no longer

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considered employed, so there is no obligation under the ACA's employer shared responsibility rules for an ALE to continue active health coverage.

In addition, ALEs that maintain coverage during a furlough must ensure that the coverage remains affordable, as defined by the ACA, to avoid penalties. Depending on the circumstances, this may require an increased employer subsidy.

COBRA and State Continuation Coverage

If active health plan coverage terminates due to a furlough or layoff, employees may have the right to continue their coverage under federal or state continuation coverage laws. The [Consolidated Omnibus Budget Reconciliation Act](#) (COBRA) is a federal law that requires covered group health plans to offer continuation coverage to employees, spouses and dependent children when their coverage would otherwise end due to certain specific events, called qualifying events. Both termination of employment and a reduction in hours of service that causes a loss of eligibility for coverage are considered COBRA-qualifying events that would entitle an employee (and any covered dependents) to elect up to 18 months of COBRA continuation coverage. Employers should provide a COBRA election notice when employees lose coverage due to layoff or furlough.

Although COBRA only applies to health plans maintained by employers with 20 or more employees, most states have their own continuation coverage laws that apply to insured group health plans of smaller employers. If state continuation coverage rights apply, employers should ensure the required notices are provided to furloughed or laid-off employees.

Group health plans can require qualified beneficiaries to pay for COBRA continuation coverage, although employers can choose to provide continuation coverage at reduced or no cost. In general, the maximum amount charged to qualified beneficiaries cannot exceed 102% of the cost to the plan for similarly situated individuals covered under the plan who have not incurred a qualifying event.

Employee Compensation Considerations

Wages Under the FLSA

In general, the FLSA only requires employers to compensate employees for hours actually worked. Therefore, employers do not need to pay wages to laid-off employees who are no longer working or on the employer's payroll, and they typically do not need to pay furloughed employees (other than payment for hours worked in the case of furloughed employees working reduced hours).

However, special considerations apply in the case of furloughed employees who are classified as exempt from overtime under the FLSA. Exempt salaried employees must be paid their full weekly salary, regardless of the number of hours they work each week. Therefore, furloughed employees who work for only a part of a given week may still be eligible to receive their full weekly salary. However, the FLSA does not require employers to compensate exempt employees for any week in which they do not perform any work, so employers may elect to furlough exempt employees by suspending or reducing their work a week at a time (for example, having employees work one week on, one week off).

In addition, furloughing exempt employees may put employees at risk of losing their exempt status (for example, reducing their annual salary to below the minimum salary threshold to qualify for an exemption). Employees who are not exempt generally receive greater wage protections, including eligibility for overtime pay for any hours worked in excess of 40 in a given workweek. Therefore, employers should consider reviewing and confirming the appropriate classification for furloughed employees to avoid violating the FLSA.

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Paid Time Off Payout

Federal law does not require employers to pay employees for accrued but unused paid time off upon termination of employment. However, some states require employers to pay employees for any accrued but unused paid time off upon termination of employment (including a layoff). Some of these states may even consider a furlough to be a termination of employment that triggers a payout of unused paid time off. Therefore, employers should carefully review applicable state laws prior to implementing a layoff or furlough to confirm whether they are subject to any such obligations.

Unemployment Compensation

Employers that continue health coverage for laid-off or furloughed employees do not automatically jeopardize their employee's eligibility for unemployment benefits. In many cases, such employees (including employees who are working reduced hours, typically a reduction of more than 50%) are eligible for unemployment benefits. Eligibility for unemployment benefits is generally determined by state unemployment insurance programs rather than federal law. Therefore, employees are encouraged to contact their state's unemployment insurance program for questions regarding eligibility and benefits.