



Employee Benefits and New Department of Labor Overtime Rules

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Employee Benefits and New Department of Labor Overtime Rules

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The ***Department of Labor's*** new *overtime rules* take effect December 1, 2016, and employers across the country are carefully reviewing and modifying their compensation and payroll practices in anticipation. As part of this preparation, employers must consider whether and how any changes to their compensation structures will affect their employee benefit plans. This post examines some of the employee benefits issues that employers should be considering as the December 1 deadline approaches.

Introduction

In a nutshell, the new overtime rules increase the salary levels at which executive, administrative, and professional workers may be considered "exempt" from overtime pay when a work week exceeds 40 hours. Initially, the standard salary level will increase from \$455 to \$913 per week (up to 10% of which may be met with nondiscretionary incentive compensation) and the total annual compensation requirement for highly compensated employee exemption will increase from \$100,000 to \$134,004 per year. In addition to these initial compensation level bumps, additional upward adjustments are scheduled to occur every three years thereafter.

Employers are responding to these changes in a number of ways. Some are raising base salaries in order to classify additional employees as "exempt". Others are planning to simply pay overtime where necessary. Others are planning to cap hours at 40 so that no overtime need

be paid, or to meet their needs with part-time workers. Regardless of the planned changes, effects on the employer's benefit plans must be considered. The following are a list of some of the key benefits issues employers should be considering as part of their analysis of the overtime rules.

1. Let's pay for this by reducing benefits!

The fact is, employers do not have unlimited cash to pay for compensation increases. The money has to come from somewhere, and benefit reductions and changes are a viable source. For example, employers might:

- Reduce or eliminate employer premium contributions towards health and welfare plans;
- Shift costs to employees or otherwise reduce costs through plan design changes, such as increased deductibles and copayments, medical management, or reduction or elimination of certain costly benefits;
- Change eligibility criteria to exclude cohorts of employees;
- Reduce or eliminate 401(k) matching or other employer contributions; or
- Reduce paid time off or other employee perks (such as subsidized child care or fitness centers, transportation subsidies, or parties).

While these options are all possible, employers should proceed with caution and consider all underlying legal requirements applicable to their benefit plans. For example, if an employer has a "safe harbor" 401(k) plan (and wants to keep "safe harbor" status), it cannot eliminate employer contributions altogether. In addition, nondiscrimination rules apply to retirement, medical, and life insurance plans; these rules are meant to ensure that the tax benefits of these plans are not skewed towards highly compensated individuals. If benefits are modified so that lower paid employees are excluded, these rules could be implicated.

2. But it's not that easy to reduce medical benefits.

Under the Affordable Care Act (ACA), large employers (generally, 50+ employees) must either offer "affordable", "minimum value" major medical coverage to full-time employees, or risk a hefty tax penalty. To sum up these complex rules for our purposes: reducing or eliminating an employer's premium contribution can affect "affordability," and changing the plan design (e.g. by eliminating certain benefits or implementing cost sharing) can affect "minimum value." In addition, regardless of whether an employee is exempt or non-exempt, he or she will be considered "full time" (must be offered coverage) if he or she works more than 30 hours per week; excluding cohorts of employees from medical coverage based on classification does not work. In other words, with respect to major medical offerings, there is only so much wiggle room, particularly for employers who are already offering the bare minimum required to avoid ACA penalties.

3. Changing compensation structures may unintentionally affect eligibility for (and amount of) benefits under existing plans.

Employers also must take care when reclassifying formerly "non-exempt" employees as "exempt" and vice versa. Reclassifying employees could cause large cohorts of employees to either gain or lose benefits, and compensation changes can in some cases affect overall benefits. Some examples include:

- **401(k) Plans.** For purposes of calculating employee elective deferrals and matching contributions, some 401(k) plans count overtime and bonuses as "compensation" and others do not. If plans do count overtime and/or bonuses, and overtime/bonuses increase, the employer's matching contribution will increase. But if plans do not count overtime, and overtime pay increases, the amount of elective deferrals and matching contributions may be skewed towards exempt

(higher paid) employees, resulting in nondiscrimination testing problems.

- **Waiting periods.** An employer's short term disability plan may impose a 5-day waiting period on non-exempt employees, but allow exempt employees to receive benefits on day one of disability. Shifts among the exempt and non-exempt groups will cause waiting periods to change, perhaps inadvertently, for some employees.
- **Premium share.** Some employers may vary health and welfare premium contributions based on compensation. If an employer decides to increase compensation to avoid paying overtime, its premium contributions may need to increase or decrease unless plan design changes are made.
- Given that plan designs are infinitely varied, the above list is not at all exhaustive. Employers are advised to review all benefit plans to identify where changes in compensation or employee reclassification may have an impact, and determine whether amendments might be in order.

4. Changing compensation in a way that results in the loss of benefits could implicate Section 510 of ERISA.

ERISA Section 510 states, in relevant part:

It shall be unlawful for any person to discharge, fine, suspend, expel, discipline, or discriminate against a participant or beneficiary for exercising any right to which he is entitled under the provisions of an employee benefit plan, [Title I of ERISA] . . . or for the purpose of interfering with the attainment of any right to which such participant may become entitled under the plan [or Title I of ERISA...].

This section has received renewed attention in the wake of the Affordable Care Act, as courts consider whether reducing hours to avoid offering medical coverage could be an ERISA 510 violation (see [*Marin v. Dave & Buster's, Inc.*](#), S.D.N.Y., No. 1:15-cv-03608, in which plaintiffs allege that the employer reduced their hours in order to exclude them from participation in its medical plan, and in doing so violated ERISA 510). Could a reduction in hours resulting in a loss of benefits trigger an ERISA 510 violation, even if the sole purpose of that hours reduction was to comply with the new overtime rules? While this theory seems tenuous, it remains to be seen whether courts will consider it.

5. When modifying benefits, don't overlook legal obligations . . .

Any modification of benefits triggers a number of ERISA and other requirements. Plan documents must be amended. The ERISA Summary Plan Description (SPD) or [wrap document](#) should be updated and re-distributed within 210 days following the close of the plan year in which the change was made or, with respect to a material reduction in services or benefits under a group medical plan, within 60 days after the date of adoption of the modification or change. A modified Summary of Benefits and Coverage (SBC) must be provided 60 days in advance of the effective date of the change if there is a material modification to a major medical plan made outside of open enrollment. Finally, [handbooks](#) and other employee communications should be kept up to date.

6. . . Or the impact on employee morale.

Just because benefits changes are legal and properly documented doesn't mean that they are going to go over well with employees. Employers must do everything they can to give employees notice of benefit changes and opportunities for employees to ask questions and be heard.

Conclusion

The DOL's new overtime rules will require many employers to make sweeping and expensive changes to their compensation practices. These changes promise to impact employee benefit plans in both intended and unintended ways. Employers are urged to conduct a thorough benefit plan analysis before making any sweeping compensation changes.

