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## 5 High-Level Issues to Consider in Shaping Your Organization's Employee Benefit Offerings

The workplace that we know today is rapidly changing. Competition for highly skilled workers is fierce, employees have become more mobile (due, in part, to alternative work arrangements or outsourcing), and there are often several generations of employees working alongside one another with different workplace approaches and perspectives. Developing employee benefit and compensation programs that are meaningful to a diverse group of workers with varied needs will become increasingly more challenging. This month's *Take 5* discusses the following five high-level issues to consider in shaping your organization's employee benefit offerings:

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1. **There Is a “Retirement Crisis” in America**
2. **Healthy Employees Are More Productive and Less Likely to Be Absent**
3. **Offer Benefits Programs that Appeal to a Multigenerational Workplace**
4. **Prudent Outsourcing Can Assist Plan Sponsors Manage Benefit Plans**
5. **Address Employee Benefits Early in Corporate Transactions**

As the workplace has changed, so has the employer-provided system of employee benefits, which has greatly evolved compared to 40 years ago, when the Employee Retirement Income Security Act (“ERISA”) was passed on September 2, 1974. Since that time alone, while the protections for benefits under ERISA have increased, the administrative, reporting, and disclosure obligations have grown. There have also been important amendments to the Internal Revenue Code (“Code”) affecting qualified retirement plans (including the addition of “Section 401(k),” pursuant to which the defined contribution plan industry developed), as well as the design of nonqualified deferred compensation plans under “Section 409A.” We have seen expanded rights to continuation of health care coverage with the Consolidated Omnibus Budget Reconciliation Act (“COBRA”), special enrollment rights, privacy and security protections under the Health Insurance Portability and Accountability Act (“HIPAA”), and a complete transformation of our health care delivery system with the Patient Protection and Affordable Care Act. We have also experienced tremendous changes to executive

compensation practices, most recently as a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

In light of the evolution of these legal developments and the probability of continued lawmaking in this regard, employers will continue to face incredible challenges to maintain their benefits and compensation programs in compliance with applicable laws, manage costs, and design programs that are of perceived value to employees. Without this effort on the part of employers, however, employees would either be fully dependent on themselves to determine how to save for their retirement years and insure their health and welfare needs, or dependent on a social welfare government system.

In order for technology, media and telecommunications (“TMT”) companies to continue to drive innovation, comprehensive compensation and benefits packages that attract employees with the necessary skills and experience and serve to retain them and minimize workplace disruptions should be considered. A comprehensive package will allow employees to focus on the business at hand and ease their concerns regarding their retirement, health, and welfare and will, in turn, assist the organization in securing the loyalty of its precious human capital in order to meet its business goals. Consider the following in shaping your organization’s employee benefit offerings:

## **1. There Is a “Retirement Crisis” in America**

It has been widely reported that Americans—from baby boomers, to Generation X-ers, to millennials—are facing a retirement crisis. When Senator Tom Harkin of Iowa introduced the *USA Retirement Funds Act* in January 2014, it was noted that the difference between what people have saved for retirement and what they should have saved is at least \$6.6 trillion; only one in five people have an employer-provided defined benefit pension plan, and half of workers have no plan at all.

There are many causes for the retirement crisis, including the economic downturn that commenced in 2008, the participation levels in savings vehicles and savings rates of individuals, and the movement away from the traditional employer-sponsored defined benefit pension plan. The traditional pension plan was part of the so-called “three-legged stool” of pension, social security, and personal savings. With the advent of the 401(k) plan and development of the defined contribution plan industry, many employers began to embrace the 401k plan in lieu of the defined benefit pension plan, or provided both types of plans for a period of time. Many employers also provided a matching contribution in the 401(k) plan for their employees, which, over time, many employers have frozen or eliminated from their plans. In addition, many employers have frozen or terminated their pension plans. Thus, the “three-legged stool” has evolved to be comprised of two legs that are solely dependent on the individual and one leg that is dependent on the solvency of Social Security.

In recent years, the U.S. government has been looking for ways to address the retirement savings issues with proposals for automatic enrollment and savings requirements, lifetime income options, and other features for defined contribution plans that are reminiscent of the defined benefit pension plan. President Obama also announced the introduction of the *MyRa* in 2014 as a way to encourage workers to start saving through payroll deductions and as a means to transition to longer-term options. Yet, at the same time, there are tax proposals to raise revenue by capping defined contribution plan contributions as well as to eliminate the tax benefits of sponsoring plans, proposals that deliver a mixed message on

the retirement crisis, and possible solutions. Congressional hearings also were recently held regarding the retirement crisis and proposals for pension reform. Clearly, the tax advantages of sponsoring and participating in retirement programs must be preserved, and employers should maximize their retirement vehicle offerings to the fullest extent possible.

In order to enable employees to secure their retirements, employers should consider sponsoring not only defined contribution plans but also defined benefit plans. Defined contribution plans alone, such as the 401(k) plan, are not sufficient for most workers to accumulate necessary retirement savings for various reasons. Many employees either do not voluntarily enroll in a defined contribution plan without education campaigns or do not adequately contribute to their plan. Many employers must resort to automatic enrollment designs to increase participation. Another concern is whether the employees who participate in the plans have sufficient knowledge to appropriately invest their contributions amongst the plans' investment options and that they understand the fee disclosures and costs associated with their investment options and plan services. In addition, regulators recognize that lump sum distributions are often not properly invested or saved, and there is a need for annuity payments. As a result, many employees are caught in a system where they must determine how to save and fund their own retirement accounts without sufficient knowledge or expertise in order to accumulate enough funds to last over their retirement years. While a defined contribution plan offered alone provides employees a mechanism to take some responsibility and ownership over their retirement security, a defined contribution plan offered alongside a defined benefit pension plan is more robust and can provide employees with more retirement security.

The design of a traditional defined benefit pension plan serves to remove the decision-making from the individual employee and provides them with an employer-funded, projected retirement benefit that will be payable in an income stream over the life of the employee (and surviving spouse) rather than a lump sum that might not have even accumulated adequately. It is understood that sponsoring a defined benefit pension plan is not without its challenges. Employers must meet many requirements under ERISA and the Code, including meeting plan qualification standards; minimum funding requirements; payment of premiums to the Pension Benefit Guaranty Corporation; administrative burdens; reporting and disclosure obligations; and fiduciary responsibilities. Pension plan management often requires assistance from various third parties, including actuaries, consultants, investment managers, and attorneys. Yet, with proper due diligence regarding plan designs, prudent selection of service providers that can assist with various aspects of plan administration, investment professionals who can assist in the design of sound funding strategies, training for plan fiduciaries, and economic balancing between overall salary compensation and pension contributions, pension plans can be properly managed, funded, and invested to meet the required obligations.

Employers should consider the long-term implications of dismissing the prospect of sponsoring a defined benefit pension plan alongside a defined contribution plan and engage in a thoughtful analysis of the importance of these benefits. The retirement security and diversification that can be provided by the "three-legged stool"—comprised of the employer leg (pension), government leg (social security), and individual leg (savings)—should be revisited and advocated. TMT companies should develop a comprehensive compensation and benefits strategy that is both competitive and clear in its message of total rewards to the employee. Comprehensive retirement programs will attract and retain the important human capital needed for an organization to grow and thrive, and it will build loyalty and aid employees as they strive to secure their retirements.

## 2. Healthy Employees Are More Productive and Less Likely to Be Absent

As employers continue to navigate the impact that the requirements under the Affordable Care Act have on their group health plans, there is great interest in finding ways to assist employees in achieving improved health through the use of wellness programs, which, in turn, can help save health plan costs, improve health, and reduce absenteeism. Yet, wellness programs are complex and must be analyzed not only under the Affordable Care Act and HIPAA nondiscrimination rules, but also under such laws as the Americans with Disabilities Act (“ADA”), Genetic Information Non-Discrimination Act (“GINA”), Title VII of the Civil Rights Act, the Age Discrimination in Employment Act (“ADEA”), HIPAA privacy rules, applicable state laws, the Code, and ERISA.

Health-contingent wellness programs (including “activity-only” or “outcome-based” programs) must meet several requirements in order to not discriminate based on health status (the “Five Requirements”):

- (i) **frequency of opportunity to qualify**—employees must be able to qualify for the reward at least once per year;
- (ii) **size of reward**—rewards may have a value for all health contingent programs up to 30 percent of the total cost of the annual premium for employee-only coverage (or up to 50 percent for programs to prevent or reduce tobacco use);
- (iii) **reasonable design**—a reasonable standard must be imposed to promote health or prevent disease that is not overly burdensome or a subterfuge for discrimination based on a health factor or highly suspect in method chosen to promote health or prevent disease;
- (iv) **uniform availability for all similarly situated individuals and reasonable alternative standards**—if it is unreasonably difficult due to a medical condition to meet the standard of the program or to attempt to satisfy it, an alternative must be provided or the participation in the program must be waived to obtain the reward; and
- (v) **notice of availability of reasonable alternative standards**—disclosures must be provided in all plan materials describing the program regarding the availability of alternative standards to qualify for the reward and, if applicable, the possibility of a waiver of the otherwise applicable standard.

Participatory wellness programs do not include conditions for obtaining rewards that are based on an individual attaining a standard based on a health factor, and they are not required to meet the Five Requirements. Participatory wellness programs include programs that:

- reimburse costs for gym memberships;
- offer diagnostic testing, such as those that provide a reward for taking a series of biometric tests without regard to the results;

- reimburse employees for costs of participating (or provide a reward) for participating in a smoking cessation program without regard to whether the employee quits smoking;
- provide a reward to employees for attending health education seminars; and
- provide a reward to employees who complete a health risk assessment regarding current health status without any further action required by the employee.

Any rewards provided in connection with a participatory wellness program do not count toward the current 30 and 50 percent permissible reward thresholds of health-contingent programs. Further, reasonable alternative standards do not need to be made available under participatory wellness programs.

In addition to the foregoing, wellness programs must be analyzed under many laws. Under the ADA, employers cannot discriminate against disabled employees in connection with the terms, conditions, or privileges of employment, or make disability-related inquiries or require medical exams of employees (unless job-related and consistent with business necessity). Such inquiries may be permissible under a wellness program if the program is voluntary. Under limited U.S. Equal Employment Opportunity Commission (“EEOC”) guidance, a wellness program is voluntary if employees are neither required to participate nor penalized for non-participation. In a recent case filed in Wisconsin by the EEOC, the EEOC alleged that a company penalized an employee who refused to participate in a company wellness program that required the employee to participate in medical examinations and inquiries that were not job-related or consistent with business necessity by shifting the entire cost of health care premiums to her, and then later terminated her from employment. In a second recent case, the EEOC has alleged that employees were forced to submit to biometric testing and complete a Health Risk Assessment (“HRA”) or face paying the full cost of insurance or cancellation of such insurance. From an EEOC perspective, wellness programs must be voluntary and cannot impose large penalties (such as a shift in 100 percent of premium cost, cancellation of insurance, or termination of employment) to employees who refuse to participate; however, bright-line rules regarding wellness programs are not expected to be issued by the EEOC.

A wellness program could potentially violate Title VII if it results in disparate treatment or has a disparate impact on a protected class. The program could also violate the ADEA, for example, if it can be shown that the wellness program provides financial incentives based upon health standards that are more difficult for older workers to achieve. In addition, GINA prohibits health plans from requiring individuals to complete an HRA that requests family medical history in order to receive a reward under a wellness program. If an employer offers an incentive for employees who complete an HRA that asks about an employee's family medical history, the HRA must state that any incentive will be given for completing the HRA regardless of whether the employee answers the questions seeking genetic information.

State laws can also be implicated with respect to wellness programs, including state laws on confidentiality of information and anti-discrimination and lifestyle (sometimes referred to “off-duty conduct”) laws. Any information obtained in conjunction with wellness programs should be protected under applicable federal laws regarding confidentiality, privacy, storage, and use. Service providers should be prudently selected and monitored, and any service agreements entered into should include provisions (as well as any applicable Business Associate agreement) to protect any personal information and data collected in conjunction

with the program in accordance with HIPAA and other confidentiality and data privacy laws. Employers must also determine whether the wellness program is part of their overall group health plan or, rather, whether such program constitutes a stand-alone arrangement that is subject to ERISA. Employers must also consider whether the type of reward must be taxed as income (e.g., gift cards).

Use of wellness programs may be desirable and can serve to promote a wellness culture at work, but care should be taken to ensure that the program is designed to comply with all applicable laws.

### **3. Offer Benefits Programs that Appeal to a Multigenerational Workplace**

Many companies are engaging in measures to better understand what their employees, regardless of their ages, desire in terms of employer-provided benefits. Recent studies regarding employee benefits trends actually show that millennials (a generation that began in the early 1980s), who have entered the workforce, desire a wide array of employee benefits—even more so than Generation X-ers or baby boomers. For millennials (which studies have shown came of age in a time of the protective “helicopter parents”) who have entered a workforce with student debts during a time of recession and a time when Social Security and the employer-provided system of retirement and health and welfare benefits are under increasing pressure and uncertainty, the desire for employer support and protection with regard to retirement, health, and welfare security has increased.

Millennials not only expect comprehensive retirement and health and welfare programs that provide protection and security, but also seek enhanced programs that include retirement education and planning services; access to financial planning and tax preparation services; auto, home, disability, and life insurance; access to mortgage services, tuition assistance, and online distance learning programs; training and mentoring programs; and technology allowances.

Further, whereas studies show that Generation X-ers may be more independent and value a choice in benefits where they can make selections that suit their needs, those studies also indicate that millennials prefer a more paternalistic approach to benefits that provides security and less decision-making on their part. In increasing numbers, today's workers value the assistance that their employer can provide in helping them attain retirement and health and welfare security as well as streamlined access to a wide array of insurance programs that will protect them and their families.

As mobile technologies become more prevalent, delivery methods for benefit plan information and educational tools should be considered. Many new plan services are emerging, including online investment educational tools as well as video-chat options. Regardless of which generation an employee is a member, your employees may prefer to receive benefit plan information online and enroll in benefits through their smartphones, whereas other organizations may have a majority of employees who do not prefer using such technologies. Therefore, understanding your demographics is key to developing a useful communication and administrative strategy that complies with applicable laws for delivery of any electronic disclosures and use of new technologies.

TMT companies that want to capture the hearts, minds, and loyalty of their employees, especially those of the younger generations, must take note of the different expectations of their multigenerational workers, as well as the impact that they will have on the attractiveness of an employee benefits program.

#### **4. Prudent Outsourcing Can Assist Plan Sponsors Manage Benefit Plans**

Given the complexities of administering and maintaining employee benefits programs, such as retirement and health and welfare programs, many organizations turn to outside service providers and vendors for assistance with benefit plan administration. Many plan sponsors seek to increase the amount of managerial and administrative tasks that are outsourced for both retirement and health and welfare plans, so that they can focus on their core business rather than the business of managing employee benefit plans. When plan sponsors seek to outsource certain fiduciary functions, such as plan investments, extra care is necessary to prudently select and monitor such services consistent with the sponsors' fiduciary responsibilities.

Recognizing that plan sponsors have operated under a patchwork of guidance to date concerning the attribution of their legal responsibilities vis-à-vis their outsourced providers, the Advisory Council on Employee Welfare and Pension Benefit Plans presented several recommendations to the Secretary of Labor this year regarding best practices for outsourcing employee benefit plan services. The outcome of these meetings will need to be watched closely for trends and guidelines in this regard, which can assist plan sponsors in managing their benefit plans more efficiently while gaining access to expertise, technology, and economies of scale to reduce costs. Plan sponsors need a clearer framework in order to establish the allocation of legal responsibilities between themselves and their service providers, particularly with regard to services that are fiduciary in nature. More definitive guidance is being sought with respect to several issues, including:

- (i) the types of fiduciary and non-fiduciary services that are currently outsourced and trends in that regard;
- (ii) clarification concerning the legal framework under ERISA for retaining outsourced service providers, including plan sponsor and service provider responsibilities;
- (iii) establishment of best practices in selecting and monitoring outsourced service providers, including identification of performance standards, benchmarking of costs, and mitigating conflicts of interest;
- (iv) for fiduciary services, determination of the differences between status as a fiduciary under ERISA Section 3(16), 3(21), and 3(38) and the scope of co-fiduciary liability in the outsourcing context;
- (v) standards for negotiating outsourcing service agreements with respect to termination rights, indemnification, and liability caps; and
- (vi) understanding insurance coverage and ERISA bonding practices of outsourced service providers to determine risk shifting to service providers.

It will also become increasingly more important for plan sponsors and fiduciaries to evaluate new technologies that emerge with regard to benefit plan administration, such as online enrollment and administration tools, data collection services, and the use of cloud storage. It may be necessary to engage the assistance of in-house IT and security departments to review the terms and conditions of such services, as well as attorneys to review the contractual terms of any data privacy, data breach and security, confidentiality, and software licensing provisions.

When selecting any service providers, plan sponsors and fiduciaries are required under ERISA to engage in a prudent process. With the advent of sophisticated technologies, attainment of the prudence standard may require enhanced due diligence. In some cases, a formal request-for-proposal process may be warranted as part of due diligence unless a particular service provider was previously evaluated recently. The decision-making process for selection of the service provider should be documented to protect the plan fiduciaries, and the plan fiduciaries must continue to monitor the performance of the service provider as part of its fiduciary responsibilities. The release of guidelines on the issues surrounding outsourcing should be monitored and incorporated into any selection process.

## **5. Address Employee Benefits Early in Corporate Transactions**

TMT companies drive through innovation; corporate transactions can provide TMT companies with growth opportunities. Many times, however, employee benefits issues are not front and center when parties negotiate and consummate their fast-paced deals. Thorough due diligence of employee benefits programs and compensation issues early in a transaction is necessary so that potential liabilities and pitfalls can be identified and dealt with in the transaction documents with the appropriate representations, warranties, and covenants, as well as any relevant purchase price adjustments, escrow arrangements, or terms for indemnification. Potential plan funding liabilities (e.g., pension and retiree medical) and multiemployer pension withdrawal liabilities must be analyzed and addressed. In some cases, it may be necessary to terminate plans prior to the closing of the transaction, and there will be important notifications that may need to be provided to government agencies, participants and beneficiaries, and service providers in accordance with certain timeframes. Continuation of health coverage issues may arise under COBRA that impact existing and new COBRA beneficiaries. Plan amendments may also be necessary for the acquiring company's plans in order to integrate the target employees. Aside from these plan-related concerns, executive compensation arrangements must be reviewed for payment triggers and related tax issues that may arise as a result of the transaction. This is not an exhaustive list of the benefits and compensation issues that must be considered, but it is indicative of the complexities that must be addressed.

It is also important to develop a communications strategy for the affected employees regarding their benefits and any transitional issues. Certain notices are required by law, such as defined contribution plan blackout notices, COBRA notices, and summaries of material modification. Comprehensive communications should also be provided to affected employees to answer their anticipated questions concerning all of their benefits. If a transition services agreement has been negotiated in the transaction, explain any impact to the employees, clarify plan contact information, and remind them of any deadlines to submit applicable benefit claims. Ensure that there is time to develop positive messaging to energize employees about the corporate changes and assure them that their benefits will be transitioned smoothly.

Corporate transactions are an opportunity to form new enterprises and foster innovation. It is important to consider the human element to any deal and the importance that the human capital will have to the success of the transaction. Ensure that employee benefits issues are thoroughly addressed in the deal, and let the employees know that their interests are important to the organization going forward.

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As the 21st-century workplace continues to evolve, employers can distinguish themselves as an employer of choice by developing compensation and employee benefits programs that provide meaning and value to their diverse workforce. An organization's compensation and benefits package is an important tool to attract, motivate, and retain employees and greatly influences employee loyalty, morale, and the overall caliber of the organization. The management and administration of employee benefit plans is complex, but there are professional service providers to assist plan sponsors with all facets of their programs. The time is now to develop a comprehensive strategy to deliver employee benefits in a cost-efficient manner that will enable workers to focus on their jobs and rest assured that their retirement security, health, and welfare needs are being met. If the system of employer-provided retirement and health and welfare programs collapses, we will all live and work in a very different America.

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This issue of *Take 5* was written by **Michelle Capezza**, a Member of the Firm in Epstein Becker Green's New York office. For additional information about the issues discussed above, please contact the Epstein Becker Green attorney who regularly handles your legal matters or the author of this *Take 5*:

**Michelle Capezza**  
New York  
212/351-4774  
[mcapezza@ebglaw.com](mailto:mcapezza@ebglaw.com)

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