



# Employee Benefits Law Action Memo

March 2009

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## **COBRA CHANGES INCLUDED IN FEDERAL STIMULUS ACT REQUIRE IMMEDIATE ACTION**

The economic stimulus package known as the American Recovery and Reinvestment Act of 2009 ("ARRA"), and signed into law by President Obama on February 17, 2009, included important changes to the health plan continuation coverage requirements commonly known as COBRA. Immediate action by employers and plan administrators is required to comply with these new rules. Under normal COBRA rules, an individual who becomes eligible to elect COBRA continuation coverage due to the occurrence of a "qualifying event" that results in the loss of group health plan coverage (e.g., termination of employment, reduction in hours or disability) must pay the full premium cost of the continued health coverage (plus a 2% administrative charge). In general, the ARRA provides that individuals who become eligible for COBRA continuation coverage due to involuntary termination of employment between September 1, 2008 and December 31, 2009 may be eligible to pay a reduced premium equal to 35% of the generally applicable COBRA premium for up to nine months. The ARRA also provides individuals who were involuntarily terminated on or after September 1, 2008, but who previously declined COBRA continuation coverage, a second opportunity to elect COBRA continuation coverage. These rules are summarized below.

### **Who Is Eligible for the Premium Reduction?**

The ARRA provides that the premium reduction must be provided to any individual who became eligible for COBRA coverage due to the covered employee's involuntary termination of employment during the period from September 1, 2008 to December 31, 2009. The COBRA premium reduction is not limited to those employees whose involuntary termination of employment was without cause (e.g., due to a reduction in force or a plant shut-down). Instead, the premium reduction must be made available to an employee and his qualifying spouse and dependents even if the employee was terminated due to poor performance. While COBRA coverage (including the premium reduction) may be denied for an employee who is terminated for gross misconduct, employers and plan administrators should be very cautious about relying on the gross misconduct exception. Remember, each COBRA "qualified beneficiary" has an independent right to elect COBRA. Therefore, an employee's spouse or other beneficiary may elect COBRA and be eligible for the premium reduction, even if the terminated employee declines coverage.

### **How Much is the Premium Reduction and How is it Administered?**

Under the ARRA, the federal government will subsidize 65% of the amount normally required to be paid by the covered individual. The covered individual is responsible for the remaining 35%. For employer-sponsored group health plans, the employer or the plan sponsor initially pays 65% of the required premium. The employer/plan sponsor recoups the premium from the federal government in the form of an offset against its payroll tax liability. IRS guidance regarding the procedures for claiming the offset can be found at <http://www.irs.gov/newsroom/article/0,,id=204505,00.html>.

However, all or part of the subsidy will be recouped from individuals whose income exceeds certain thresholds. An individual with a modified adjusted gross income of more than \$145,000 (\$290,000 for joint filers) who receives the premium subsidy will have his or her income tax liability increased by the amount of the subsidy received. Individuals earning more than \$125,000 (\$250,000 for joint filers), but less than \$145,000 (\$290,000 for joint filers) will have a portion of subsidy received added to their income tax liability. The recapture of the subsidy can be avoided if the individual permanently waives the right to the subsidy.



## What Type of Coverage is the Premium Reduction Available For?

The premium subsidy is available for any COBRA coverage, other than continued coverage under a flexible spending arrangement. Thus, the subsidy is available for medical, dental, vision or employee assistance plan coverage continued under COBRA. Under normal COBRA rules, an individual is permitted to continue the coverage the individual had prior to the qualifying event (i.e., the coverage the individual had as an active employee). Under the ARRA, an employer may, but is not required to, allow individuals to choose a different coverage option available under the plan, provided that certain requirements are satisfied. If the employer chooses to provide the option to elect different coverage, notice of this election right must be provided. The individual must be given a 90 day period (measured from the date that the notice is given) to elect the different coverage. It is unclear how this 90 day period interacts with the general rule that an election to continue coverage under COBRA be made within 60 days of the date that the individual is provided notice of his or her COBRA rights.

## How Long Does the Premium Reduction Last?

The premium reduction will last for up to nine months. After the expiration of the subsidy, the covered individual will be responsible for the full amount of the COBRA premium, in accordance with general COBRA rules. However, entitlement to the COBRA subsidy ends when the individual becomes eligible for certain other group health plan coverage or Medicare, regardless of whether the individual actually enrolls in the other coverage. The ARRA requires that an individual receiving the COBRA subsidy provide timely notice of eligibility for coverage that would terminate the subsidy. A failure to provide such notice could result in a penalty equal to 110% of the subsidy received after the individual became eligible for the other coverage.

However, not all group health plan coverage will terminate the subsidy. Eligibility for coverage consisting of only dental, vision, counseling or referral services, coverage under a flexible spending arrangement, or coverage of treatment furnished at an on-site facility providing only first-aid, prevention or wellness care, does not trigger the termination of the subsidy.

## What are the New Notice Obligations?

Under the ARRA, the COBRA notice required to be provided to a qualified beneficiary must include (1) the forms necessary for establishing eligibility for the COBRA subsidy, (2) contact information for the plan administrator and any other persons maintaining relevant information regarding the subsidy, (3) a description of the right to the COBRA subsidy and any restrictions on such right, (4) a description of the individual's obligation to notify the plan providing COBRA of eligibility for other coverage and the penalty for failing to provide such notice, and (5) a description of the right to elect different coverage, if offered by the plan. Model forms issued by the U.S. Department of Labor are available at [www.dol.gov/ebsa/COBRAModelNotice.html](http://www.dol.gov/ebsa/COBRAModelNotice.html).

For an individual whose qualifying event occurs on or after February 17, 2009, the additional notice information must be included in the COBRA notice provided under the normal COBRA timing rules. For an individual currently covered by COBRA whose qualifying event occurred between September 1, 2008 and February 16, 2009, the additional notice information must be provided no later than April 18, 2009.

A special rule applies to individuals who became qualified beneficiaries due to involuntary termination of employment on or after September 1, 2008 who either declined COBRA coverage or initially elected COBRA coverage but let it lapse (e.g., due to nonpayment of the required premium). These individuals must be provided with a new opportunity to elect COBRA coverage (and receive the benefit of the COBRA subsidy). Notice of this new election opportunity must be provided to affected individuals no later than April 18, 2009. If an affected individual elects COBRA coverage within 60 days after the date the notice is provided, the COBRA coverage will commence as of the first "period of coverage" that begins on or after February 17, 2009. Generally, this means that, for a plan that charges COBRA premiums on a monthly basis, the COBRA coverage would be effective as of March 1, 2009. However, the length of the COBRA coverage period is determined from the date of the original qualifying event (i.e., the date of the involuntary termination).

## What Should Employers Be Doing Now?

Given that notices must be provided no later than April 18, 2009, employers and plan administrators should take immediate action to comply with the new COBRA rules. These actions should include (1) identifying those individuals (including spouses and dependents) who were eligible to elect COBRA due to involuntary termination of employment on or after September 1, 2008, (2) developing the notices required to be provided and implementing procedures to deliver them, (3) consulting with payroll administrators/providers on procedures to claim credit for the subsidy on payroll tax filings, and (4) consulting with insurers, third party administrators and other involved parties to insure that the ARRA's COBRA provisions are being followed.

If you have any questions about this memorandum, please contact Aaron Pierce in our Syracuse office (315-218-8635, [apierce@bsk.com](mailto:apierce@bsk.com)) or any of the other members of our Employee Benefits and Executive Compensation Practice Group listed below.

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