

# NEW COBRA RULES AS A RESULT OF THE ECONOMIC STIMULUS PACKAGE

## WHAT IS IT?

The American Recovery and Reinvestment Act of 2009 (the Act) is effective February 17, 2009, and contains significant modifications of the COBRA continuation coverage rules. This **Conrad Siegel Actuaries** update provides general guidance on what employers need to know about the changes to COBRA for employees who are involuntarily terminated.

Generally, the Act provides qualified COBRA participants with a 65 percent federal subsidy for up to nine (9) months of COBRA coverage for individuals who became eligible for COBRA coverage from September 1, 2008 through December 31, 2009, due to involuntary termination of employment. The Act permits these COBRA individuals to satisfy their COBRA premium obligation by paying only 35 percent of the premium. The employer associated with the COBRA benefit is required to provide the subsidy on behalf of the federal government and then to reimburse itself through a payroll tax credit.

The group health plan sponsor is directed to pay reduced payroll taxes in the aggregate amount of 65 percent of the premium for all individuals who opt into the provision or, if COBRA subsidy exceeds payroll taxes, employers will be reimbursed directly through a program established by the Department of Treasury. Any overstatement of the subsidy reimbursement will be treated as an underpayment of payroll taxes. The entity to whom COBRA premiums are payable is the entity entitled to the government reimbursement subsidy. In the case of a multi-employer plan, the entity entitled to the subsidy is the plan. In the case of any other group health plan, the entitled entity is the employer who maintains the plan.

The program is mandatory for employers required to offer COBRA continuation health coverage.

## WHO QUALIFIES FOR THE SUBSIDY?

Individuals who are qualified beneficiaries under COBRA are entitled to the subsidy if they (1) become eligible for COBRA between September 1, 2008 and December 31, 2009, by reason of an involuntary termination of employment and (2) elect COBRA. Temporary COBRA premium assistance applies to former covered employees, spouses and dependents. These individuals are referred to as "assistance eligible individuals." Thus, there is a closed class of individuals who can be entitled to the subsidy by electing COBRA. This closed class consists of:

- (1) Individuals who are currently covered by COBRA by reason of an involuntary termination on or after September 1, 2008;
- (2) Individuals who were previously eligible for COBRA coverage by reason of an involuntary termination on or after September 1, 2008, but did not elect COBRA;
- (3) Individuals who were previously eligible for COBRA coverage by reason of an involuntary termination on or after September 1, 2008, elected COBRA, but are no longer covered as of the date of enactment (because, for example, the individual did not pay the required premium); and
- (4) Other individuals who are eligible for COBRA coverage by reason of an involuntary termination during the September 1, 2008, through December 31, 2009 period.

## INCOME LIMITS

Premium subsidies are phased out for individual taxpayers with modified adjusted gross incomes between \$125,000 and \$145,000 (single), and \$250,000 and \$290,000 (joint filers), for the taxable year. High income individuals may waive assistance to avoid having to pay back 100% the subsidy if income exceeds \$145,000 (single) and \$290,000 (joint filers).

## WHAT IS AN INVOLUNTARY TERMINATION OF EMPLOYMENT?

Neither the Act nor legislative history provides any guidance on this issue. However, an involuntary termination may be safely interpreted as any termination that is not voluntary. Additionally, the Act does not modify current law under which an individual who is terminated by reason of gross misconduct is not eligible to elect COBRA coverage.

## WHAT COVERAGE DOES THE SUBSIDY APPLY TO?

The subsidy applies to all COBRA continuation coverage under the provisions of the Code, ERISA and plans under the Public Health Services Act (PHSA) with the exception of health flexible spending arrangements.

## WHEN DOES THE SUBSIDIZED COVERAGE BEGIN?

Assistance eligible individuals who are able to take advantage of the "second chance" election of COBRA coverage will not receive retroactive coverage. Instead, their coverage and subsidy are to commence with the first period of coverage beginning on or after the date of the law's enactment. The Act defines "period of coverage" as "a monthly or shorter period of coverage with respect to which premiums are charged with respect to such coverage." Thus, if COBRA premiums are charged on a monthly basis, as is the norm, the subsidy is to begin as of March 1, 2009.

## WHEN WOULD THE SUBSIDIZED COVERAGE END?

The COBRA premium subsidy ends upon the earliest of the following:

- (1) Nine (9) months after it starts,
- (2) The date the individual's COBRA coverage ends, or
- (3) The individual's eligibility for coverage under any other group health plan, including eligibility under a spouse's health plan (other than non-core coverage) or eligibility for Medicare

COBRA qualified beneficiaries receiving the subsidy must notify the group health plan in writing when they become eligible for other coverage, or face a penalty (110% of the premium reduction).

## SPECIAL COBRA ELECTION PERIOD

The Act creates a special COBRA election period for individuals who did not elect COBRA during their original election period that occurred sometime on or after September 1, 2008, or are currently in their COBRA election period and have not made their COBRA election as of the date of the enactment. This special COBRA election period begins with the enactment date of the Act and ends sixty (60) days after the notice of availability of premium subsidy is provided by the plan sponsor. The enactment date of the Act is the date the President signed the legislation, February 17, 2009.

## NEW NOTICE REQUIREMENTS

The Act requires that a new notice must be provided by plan administrators within sixty (60) days after the Act is enacted to all workers who were let go since September 1, 2008, and became eligible for COBRA. The purpose of the notice is to inform these former workers of their new opportunity to elect COBRA and receive a subsidy from the federal government of 65 percent of the COBRA premium. The Department of Labor is to make Model Notices available not later than thirty (30) days after the date of the enactment of the Act.

## SPECIAL OPTION TO OFFER LESS EXPENSIVE COVERAGE

Employers providing COBRA benefits will be able to allow those electing COBRA to choose from other, less expensive, insurance options at the time of the qualifying event. Due to the hardship of losing their jobs, many laid-off individuals may not be able to afford COBRA coverage, even at a 65 percent discount. The Act provides an option to plan sponsors to offer group coverage that is no more expensive than COBRA coverage. In this regard, it appears that the determination of whether coverage is less expensive is based on the premium charged to the individual, not the total cost of coverage. Such alternative coverage also must be offered to active employees. The alternative coverage must not consist of the following non-core coverages: solely dental, vision, counseling, referral services (or a combination thereof); coverage under a health flexible spending arrangement or a health reimbursement arrangement; or coverage for treatment that is furnished in an on-site medical facility maintained by the employer that consists primarily of first-aid services, prevention and wellness care or similar care (or a combination thereof).

## ANNUAL REPORTING OBLIGATIONS

Plan sponsors will be required to submit reports to the Secretary of the Treasury detailing the amount of payroll taxes offset and the subsidy provided to assistance eligible individuals (likely on a Form W-2). There is also a requirement that plan sponsors provide “attestations of involuntary terminations” to support the claim.

## GRACE PERIOD

Due to the immediacy of application of the new COBRA rules, the Act provides a grace period for employers or COBRA administrators who are unable to modify March or April COBRA bills for assistance eligible individuals in time to reflect the 65% subsidy. The grace period permits charging the full COBRA premium for two (2) billing periods, followed by an appropriate credit in subsequent billing periods equal to the missed 65 percent subsidy or, alternatively, a reimbursement to the assistance eligible individual. Special rules apply if it is apparent or becomes apparent that the credit cannot be used by the assistance eligible individual within 180 days.

## MISCELLANEOUS

- Premium subsidy is not includible in the income of the individual receiving it.
- The Act assists terminated workers to avoid triggering a 63-day break in coverage for HIPAA creditable coverage purposes. The time period beginning on the date of the qualifying event and ending with the day before the day of enactment of the Act will be disregarded for purposes of determining the 63-day break in coverage.
- The Social Security trust fund is held harmless from payroll tax offsets that are permitted under the program.
- Individuals receiving the subsidy are not eligible for the health care tax credit under Code Section 35.
- Subsidy denials are subject to fifteen (15) day reviews by the Secretary of Labor on a de novo basis.
- For purposes of determining the gross income of the employer and any welfare benefit plan, the subsidy is treated as an employee contribution.

## NEXT STEPS

The new COBRA rules have significant implications for plan sponsors. Employers should be prepared to implement the new provisions promptly by:

- Determining how to identify former employees who must receive notice about the subsidy and new enrollment opportunity. Unless relief is provided through implementing guidance, the notice will have to be provided to all persons eligible for COBRA and not just terminated employees.
- Updating COBRA notices and SPD's to include information about the subsidy and new enrollment rights.
- Offering a new enrollment period to subsidy-eligible individuals who previously declined COBRA coverage.
- Developing procedures for complying with the subsidy mechanism and receiving an offset or reimbursement from the federal government.
- Working with COBRA administrators and other appropriate vendors to develop systems and procedures for tracking subsidy-eligible individuals and eligibility periods for those who enroll in COBRA during the new enrollment period.
- Consulting with health actuaries to determine any changes to COBRA rates or Statement of Financial Accounting Standards (SFAS) 112 liabilities that may result from the increased COBRA participation and claims. Note that current COBRA rules prohibit employers from increasing premiums during their current twelve (12) month determination period.

For more information on complying with the new COBRA rules, contact the **Conrad Siegel Actuaries Health and Welfare Compliance Committee** at 717-652-5633 or email the committee at [hwcompliance@conradsiegel.com](mailto:hwcompliance@conradsiegel.com).

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