Changes to COBRA as a Result of the Economic Stimulus Bill

I. INTRODUCTION

On February 17, 2009, President Barack Obama signed into law the economic stimulus bill, which is formally titled the American Recovery and Reinvestment Act of 2009 (the "Act"). Among the Act's many provisions are several amendments to the Consolidated Omnibus Budget Reconciliation Act of 1985 ("COBRA") which, among other things, governs the requirements for continued health care coverage of individuals following various qualifying events such as an involuntary loss of employment or reduction of work hours.

The major effect of the Act on COBRA is the creation of a temporary federal subsidy for continuation premiums which affects employer notice requirements and payroll tax administration. This enactment has immediate implications for employers.

Though the Department of Labor and Internal Revenue Service are still developing the rules that govern implementation of these changes, what follows is the guidance we do currently have and about which all employers should be aware.

II. DETAILS OF THE SUBSIDY

- Eligible individuals will be required to pay just 35% of the applicable COBRA premiums for continuation coverage. Employers will be required to pay the remaining 65% for the applicable premiums. The 65% will be reimbursed by the federal government through quarterly payroll reporting beginning with the first quarterly return due on April 30, 2009.
- *Note*: The "applicable COBRA premium" is calculated as the amount an eligible individual would have to pay after discounting any amount which the employer may have offered to cover as part of a separation agreement.
- Subsidy lasts until the earliest of the following events: (1) a 9-month period, (2) the expiration of the continuation coverage period under COBRA, or (3) the individual becomes eligible for other group medical coverage (e.g. through a spouse, new job, or Medicare).
- The subsidy does not extend the COBRA coverage period.
- The premium reduction applies to periods of coverage beginning on or after February 17, 2009. (A "period of coverage" is a month or shorter period of time for which the plan charges a COBRA premium). Since the majority of plans collect COBRA payments on a monthly basis, the premium reduction starts on March 1, 2009 in most cases.
- Eligible individuals enrolled in COBRA coverage are not entitled to a refund for 65% of the premiums they have paid since September 2008 but prior to February 17, 2009. If an eligible individual paid in full for COBRA coverage on or after February 17, 2009, they are entitled to a refund or credit against future payments.

III. EMPLOYERS AND PLANS COVERED BY THESE CHANGES

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- All employers who sponsor a group health plan covered under COBRA (20 or more employees).
- All Massachusetts employers who sponsor a group health plan covered by MA "Mini-COBRA" (2-19 employees).
- Applies to medical, dental and vision plans but not flexible spending accounts.

IV. ELIGIBILITY OF PARTICIPANTS

Individuals eligible for the subsidy are those who become eligible for COBRA continuation coverage as a result of involuntary termination between September 1, 2008 and December 31, 2009 and who elect coverage. (See also special extended election opportunity described below).

The following is a summary of recent directives issued by the IRS and DOL clarifying the definition of "involuntary termination" for purposes of the subsidy:

Involuntary Termination
— Termination of employment, which includes a lay-off
— Reduction in hours to zero
— Employer's failure to renew contract if employee was willing and able to do so
— Voluntary retirement if employee knew employer would have terminated his or her services
— Lockout initiated by employer
— Employee's resignation if due to employer's action causing "material negative change in the employment relationship for the employee"
— Employee's resignation due to "material change in the geographic location of employment for the employee" *Not Involuntary Termination*
— Termination of employment due to gross misconduct
— Reduction in hours (other than to zero)
— Death
— Work stoppage
The subsidy begins to phase out for single taxpayers with an annual adjusted gross income of $125,000 ($250,000 for joint filers) and is eliminated entirely at $145,000 ($290,000 for joint filers).

V. SPECIAL EXTENDED ELECTION OPPORTUNITY

- Eligible individuals involuntarily terminated between September 1, 2008 and February 16, 2009 who were eligible for COBRA but did not elect COBRA (or did elect it and subsequently dropped it), have a new opportunity to enroll now.
- Employer must provide those eligible individuals with notice of this opportunity by April 18, 2009. Eligible individual has 60 days from the date the notice is received to elect coverage.
- Therefore, the extended election period begins on the date of enactment of the Act (February 17, 2009) and ends 60 days after the extended election notice is provided to the eligible individuals. Coverage will commence with the first period of coverage beginning on or after March 1. *For example: eligible individual terminated on September 30, 2008 making a timely election during the extended election period will generally will be entitled to COBRA continuation coverage prospectively beginning on March 1, 2009, although the 18-month*

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coverage period is measured from October 1, 2008.

- Remember, the usual applicable COBRA period of 18 months from the qualifying event is not extended.
- *This is not available pursuant to Massachusetts Mini-COBRA.*

VI. OPTION TO SWITCH TO LOWER-COST PLAN

Employer has the *option* (not a mandate) of allowing eligible individuals to elect continuation coverage with a lower premium health plan than the one he or she was enrolled in at the time of the qualifying event.

The different coverage cannot be coverage that provides only vision, dental, counseling or referral services, a health flexible spending account, or coverage for treatment that is provided at an on-site facility maintained by the employer.

The lower cost option must be one currently offered to active employees.

VII. SEPARATION AGREEMENTS

An employer's agreement to pay for some or all of an employee's premium as part of a separation agreement affects the availability of the subsidy. Guidance recently issued by the DOL and IRS explains the various factors that determine the application of the subsidy, which are best exemplified by the two following scenarios:Scenario A: Employee is involuntarily terminated on March 1, 2009. As part of the severance, Employer offers to pay 100% of Employee's health coverage for 3 months. *Though the qualifying event is on March 1, 2009, Employer considers the loss of coverage to be June 1, 2009, which means Employee becomes eligible for COBRA coverage as of June 1, 2009*. Accordingly, Employer gets no subsidy for that 3-month period and then Employee gets 9 months of subsidy as of June 1, 2009.

Scenario B: Employee is involuntarily terminated on March 1, 2009. As part of the severance, Employer offers to pay 100% of Employee's health coverage for 3 months. *Employer considers the qualifying event and the loss of coverage to be March 1, 2009.* Accordingly, Employer gets no subsidy for that 3-month period and Employee gets 6 months of subsidy as of June 1, 2009.

Note: the difference here is a result of whether the Employer treats the provision of health coverage as deferring the loss of coverage. In making this determination, it is important to ensure that your summary plan description, COBRA notice and election form, and insurance carrier certificate all are all consistent with your treatment of when the loss of coverage occurs.

VIII. EMPLOYER NOTICE REQUIREMENTS

On March 19, 2009, the Department of Labor published model notices. (Copies are attached and you can find them at www.dol.gov/ebsa/COBRA). There are four types:• General Notice (Full version): This form is for qualified beneficiaries who have not yet received an election notice (or did receive one after February 17, 2008 that did not include subsidy information) and had or have a qualifying event between September 1, 2008 and December 31, 2009.

- General Notice (Abbreviated version): This form includes the same information as the full

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version regarding the availability of the premium reduction and other rights under the Act, but does not include the COBRA coverage election information. It may be sent in lieu of the full version to individuals who experienced a qualifying event during on or after September 1, 2008, have already elected COBRA coverage, and still have it.

Note: one of these general notices (depending on the particular situation) must be provided to all who had a qualifying event, regardless of the type (in other words, regardless of whether employer deems the qualifying event to amount to involuntary termination).

- Notice in Connection with Extended Election Period: This form is for qualified beneficiaries who would be eligible for the subsidy but are not currently enrolled in COBRA and had a qualifying event between September 1, 2008 and February 16, 2009. Remember, this does not apply to MA Mini-COBRA.
- Alternative Notice: This form is for insurance issuers in states with continuation requirements, such as MA Mini-COBRA; provide this form to persons eligible to continuation under the state law.

IX. EMPLOYER REIMBURSEMENT

Under Federal COBRA, employers are reimbursed for the COBRA subsidy by a credit towards Federal payroll taxes:

- COBRA beneficiary pays 35%
- Employer adds balance and sends to carrier
- Employer is reimbursed via offset

Under Massachusetts Mini-COBRA, still working it out but best prediction:

- COBRA beneficiary pays 35%
- Employer sends only that amount to carrier
- Carrier reimburses itself the same way employer will under Federal COBRA

X. WHAT EMPLOYERS SHOULD DO NOW

- Send general notice to all employees who experienced a qualifying event from September 1, 2008 to date.
- Determine if the company has involuntarily terminated anyone since September 1, 2008.
- Determine whether you have individuals eligible for the subsidy.
- Decide whether you will choose to allow eligible individuals to elect a less-expensive health plan option if they elect COBRA now.
- Issue the necessary notices, particularly the one required by April 18, 2009 for the special election opportunity.
- For employees who did or will receive severance including health care payments, ensure that your summary plan description, COBRA notice and election form, and insurance carrier certificate all are all consistent with your treatment of when the loss of coverage occurs.
- Contact your tax advisors and COBRA plan administrators to ensure compliance and

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reimbursement.

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