NEWSSTAND

COBRA Premium Subsidy Included in American Recovery and Reinvestment Act of 2009

Spring 2009

Recognizing that few laid-off employees can afford to continue health coverage under the Consolidated Omnibus Budget Reconciliation Act (COBRA), laid-off employees will now be eligible for a temporary reduction in their COBRA premiums under the American Recovery and Reinvestment Act of 2009 (the "Act").

The Act creates a federal subsidy that will cover 65% of the COBRA premium for a nine-month period, with employees paying only 35%, rather than 102%, of the COBRA premium. Employers will be able to recoup the 65% subsidy from the federal government in the form of a credit against federal payroll taxes. The subsidy applies to COBRA premiums paid on or after March 1, 2009.

Eligibility for Premium Subsidy
Employees (and their qualified beneficiaries) who lose health coverage due to the employee's involuntary termination of employment between September 1, 2008 and December 31, 2009 are eligible for the premium subsidy. The subsidy does not apply to other COBRA qualifying events such as divorce, a reduction in hours or a dependent child aging out of eligibility.

According to the IRS, an involuntary termination is a termination where the employer exercises its unilateral authority to terminate employment even though the employee remains willing and able to work. An involuntary termination includes a lay-off with recall rights, a temporary furlough period or other suspension of employment in which the individual's work hours are reduced to zero, the non-renewal of an employment agreement, and certain "good reason" terminations if the employer action causes a material negative change in the employment relationship for the employee. Further, an employee-elected termination in return for a severance or retirement incentive package will be considered an involuntary termination where, absent the employee-elected termination, the employer would have terminated the employee's employment and the employee knew that he or she would have been terminated.

Amount of Premium Subsidy
Subsidy-eligible individuals who elect COBRA coverage will be responsible for paying 35% of the COBRA premium. Employers are required to pay the remaining 65% of the premium and will be reimbursed for such amount in the form of a credit against wage withholding and FICA payroll taxes.

The premium used to determine the 35% share that must be paid by (or on behalf of) a subsidy-eligible individual is the cost that would be charged for COBRA continuation coverage if the individual was not eligible for the subsidy. For example, if, without regard to the subsidy, the individual is required to pay the standard COBRA rate of 102% of the applicable premium, the individual will be required to pay 35% of the 102%. However, if the premium actually charged is less than the maximum COBRA premium because, for example, the employer subsidizes all or part of the COBRA cost, the subsidy-eligible employee will pay 35% of the amount actually charged (and the employer will be reimbursed for 65% of the amount actually charged to the individual). Employers should consider eliminating voluntary subsidies for involuntary terminations through December 31, 2009 in order to take full advantage of the COBRA premium subsidy.

The COBRA premium subsidy is phased out for subsidy-eligible individuals with adjusted gross incomes beginning at $125,000 ($250,000 for joint filers) and eliminated for subsidy-eligible individuals with adjusted gross incomes of $145,000 or more ($290,000 for joint filers). Individuals who receive the COBRA subsidy during a year in which they exceed these income limits will be required to repay the subsidy in the form of an additional tax on their tax return. As a result of this income limitation, these "high income individuals" may make a permanent election to waive the subsidy.

Duration of Premium Subsidy

The subsidy is available with respect to premiums paid on or after March 1, 2009, and lasts for up to nine months, ending earlier if the subsidy-eligible individual becomes eligible for coverage under another group health plan or Medicare. The individual is required to notify the group health plan when he or she becomes eligible for other group health coverage or Medicare. If the subsidy-eligible individual fails to notify the plan in a timely manner, the individual is liable for a penalty equal to 110% of the subsidy that is provided after eligibility terminates.

Note that eligibility for the premium subsidy ends (but not COBRA coverage) when the subsidy-eligible individual becomes eligible for other coverage, even if the individual does not enroll in, or become covered by, such other coverage. COBRA coverage ends when the qualified beneficiary actually becomes covered by another health plan.

Because this new legislation becomes effective immediately, individuals who are eligible for the premium subsidy may have already paid the full COBRA premium for March and/or April 2009. The Act entitles any subsidy-eligible individual who paid more than 35% of the COBRA premium amount during the first two coverage periods following enactment of the Act to reimbursement from the employer for the excess over the amount which the individual is required to pay, or to a credit of that amount against future COBRA premium payments. For example, if a subsidy-eligible individual paid the entire COBRA premium for March 2009, the individual may receive a refund or credit equal to 65% of the COBRA premium.

Special COBRA Election

Plans must provide a second COBRA election to qualified beneficiaries who lost group health plan coverage as a result of a covered employee's involuntary termination on or between September 1, 2008 and February 16, 2009 and who did not elect COBRA during their initial COBRA election period or elected COBRA but discontinued it. Such individuals will have 60 days in which to elect COBRA coverage. If elected during this special election period, COBRA coverage will begin on March 1, 2009 (the first period of coverage beginning on or after the enactment of the Act) rather than the date of the employment termination, but will not extend beyond the original COBRA period, measured from the date of the employment termination. For example, a subsidy-eligible individual terminated on November 30, 2008 who makes a timely election during this special COBRA election period will be entitled to COBRA coverage beginning March 1, 2009 and ending May 31, 2010 (18 months from November 30, 2008).

Option to Change Coverage

Under COBRA, qualified beneficiaries must be offered the same coverage they had at the time of their qualifying event and cannot change their coverage until the next open enrollment period. The Act permits employers to offer subsidy-eligible individuals the opportunity to elect COBRA coverage under the benefit option in which he or she was enrolled at the time of the qualifying event or to change to a lower-cost health plan option offered to active employees. Subsidy-eligible individuals must make this change within 90 days after receiving notification to elect a different option.

New COBRA Notices

Plans must provide individuals who become eligible for COBRA coverage between September 1, 2008 and December 31, 2009 with notices explaining the availability of the premium subsidy and the option to enroll in different health plan coverage, if permitted by the employer. The Department of Labor recently released model COBRA notices to assist employers and health plans in complying with this notice requirement. The model notices are available at http://www.dol.gov/ebsa/COBRAmodelnotice.html.

- ***General Notice – Full Version***
  This notice should be sent to all qualified beneficiaries (not only covered employees) who experienced a qualifying event between September 1, 2008 and December 31, 2009 and who have not previously received a COBRA notice and election

form, regardless of the type of the qualifying event. This full version model notice contains information on the COBRA premium subsidy as well as general information contained in a COBRA election notice.

- ***General Notice – Abbreviated Version***
  The abbreviated version of the General Notice should be sent to COBRA qualified beneficiaries who had a qualifying event on or after September 1, 2008, have already elected COBRA coverage and still have that coverage. This abbreviated version addresses only the subsidy and may be provided in lieu of the full version.
- ***Notice of Second Election Period***
  This notice should be sent to any qualified beneficiary who lost group health plan coverage as a result of a covered employee's involuntary termination and who did not elect COBRA or elected COBRA but subsequently let it lapse. This notice includes information about the second COBRA election opportunity as well as the COBRA premium subsidy.

Reporting Requirements for Employers

The Act requires employers to initially pay the 65% premium subsidy and recoup such amount through reduced federal payroll tax payments. These payroll taxes include federal income tax withholding as well as the employer and employee share of FICA. If the amount of the subsidy paid by the employer exceeds the amount of the employer's liability for these federal payroll taxes, the employer will receive a direct payment from the federal government.

Employers will be required to file reports relating to the subsidy, including attestations that each employee receiving the subsidy was involuntarily terminated, calculation of the offset, the amount of the subsidy provided to each individual and information as to whether the subsidy is for individual or family coverage.

Conclusion

These new COBRA requirements require employers to take immediate action, identifying all former employees who must receive notice of the premium subsidy, offering the special COBRA election period to those subsidy-eligible individuals who previously declined COBRA coverage, revising COBRA communications materials and coordinating with COBRA administrators and payroll providers to develop systems and procedures for recouping the federal subsidy.