



New COBRA Rules Require Immediate Action

Overview

On February 17, 2009 President Obama signed the American Recovery and Reinvestment Act of 2009 (the Act).

Under the Act, a group health plan cannot require a COBRA qualified beneficiary who is an assistance eligible individual (AEI) to pay more than 35% of the premium for COBRA coverage.¹ A health flexible spending arrangement under a cafeteria plan is not subject to the new law. If the plan is subject to federal COBRA (i.e., plans maintained by private sector employers with 20 or more employees and state and local governments), the employer is responsible for the remaining 65 percent which it may recoup by claiming a credit on its quarterly employment tax return.²

The premium subsidy is available for periods of COBRA coverage beginning on or after February 17, 2009, and can last up to nine months. The subsidy will end before the expiration of the nine-month period if the individual becomes eligible for coverage under another group health plan (other than certain group health plans, such as stand-alone dental, vision, and EAP plans and health FSAs) or Medicare, or his or her COBRA coverage ends, whichever is first to occur. Under the Act, an AEI must notify the plan if he or she becomes ineligible for the subsidy. The penalty for failing to do so is 110 percent of the subsidy received by the individual after the individual was no longer eligible. As noted, an individual's mere eligibility for coverage under another group health plan will render the individual ineligible for the subsidy (i.e., the individual is ineligible *regardless of whether the individual actually enrolls in the other coverage*). The Act's legislative history indicates that an individual is considered to be ineligible for the subsidy if the individual is eligible to enroll in his or her spouse's group health plan coverage.

This client alert explains the requirements of the Act and the steps employers should take to ensure compliance with its requirements. In addition, employers will want to review their severance plans to determine the impact, if any, the Act will have on health plan benefits included in the plans.

Who Is an Assistance Eligible Individual (AEI)

An AEI is a qualified beneficiary (as defined by COBRA) who (a) becomes eligible for COBRA on or after September 1, 2008 and on or before December 31, 2009 as a result of a qualifying event that is an involuntary loss of employment and that occurs during that period and (b) elects COBRA coverage when first offered or during the extended election period created by the Act (discussed below). AEIs who are eligible for other group health coverage or for Medicare are not eligible for the premium subsidy. Note, if a covered employee is denied COBRA because his or her termination resulted from gross misconduct, the covered employee's loss of employment is not a qualifying event; therefore, neither the covered employee nor his or her covered spouse or dependent child can be an AEI.

Who is a Qualified Beneficiary

When the qualifying event is termination of employment, each of the following individuals is a qualified beneficiary under COBRA: (a) the covered employee, (b) the covered employee's spouse (as defined by federal law) and his or her dependent children (as defined by the plan), if covered under the plan on the day before the qualifying event, and (c) any child born to or placed for adoption with the former employee during the period of COBRA coverage. Thus, even if the covered employee does not elect COBRA, a covered spouse or child of the covered employee may qualify for the subsidy if they elect COBRA.

High Income Individuals

If the premium reduction is applied to the cost of COBRA coverage for a high income individual, his or her spouse, or any or his or her dependent children and the individual's modified adjusted gross income exceeds \$145,000 (or \$290,000 for joint filers), then the high income individual must repay the amount of the premium subsidy. The mechanism for repayment is an increase in the individual's income tax liability for the year equal to the amount by which the premium was reduced. For individuals with adjusted gross income between \$125,000 and \$145,000 (or \$250,000 and \$290,000 for joint filers), the recapture amount is reduced proportionately. An individual may irrevocably elect to waive the right to the

premium subsidy. An AEI who is certain the modified adjusted gross income limit will prevent entitlement to the subsidy may reasonably choose to do so.

Extended Election Period

The reach-back provision of the Act creates a category of qualified beneficiaries referred to as potential AEIs. A potential AEI is a qualified beneficiary who would be an AEI if he or she had a COBRA election in effect on February 17, 2009. This includes individuals who did not have a COBRA election in effect as of that date because they did not elect it at the time of the qualifying event (or elected it but allowed it to lapse). To enable these individuals to become AEIs, plans must offer them another opportunity to elect COBRA. Potential AEIs must be notified of their election rights by April 18, 2009, after which they will have a period of 60 days to enroll in subsidized COBRA coverage. If elected, COBRA coverage (and the subsidy) begins with the first period of coverage beginning on or after February 17, 2009. COBRA coverage will end when it would have ended if COBRA had been elected at the time of the qualifying event.

How to Calculate the Subsidy

Under COBRA, a plan may require a qualified beneficiary to pay 102 percent of the applicable premium as a condition of maintaining COBRA coverage, and in our experience most plans require full payment in most situations.³ When this is the case, the subsidy is 65 percent of the plan's COBRA premium (including the administrative surcharge). It is not uncommon, however, for employers to subsidize a displaced employee's COBRA premium for a fixed period of time to make it easier for the employee to keep his or her employer-sponsored coverage. Where an employer provides a COBRA subsidy, the federal subsidy is based on the amount of the COBRA premium the employee is required to pay. For example, if the COBRA premium is \$1,000 per month (including the 2 percent administrative fee), and the employer agrees to pay 80 percent (\$800) as part of an involuntary separation plan, an AEI cannot be required to pay more than \$70 (35 percent of \$200). The employer would pay \$130 (65 percent of \$200) and would recoup the payment by claiming a \$130 credit against its payroll taxes. This means that for periods of COBRA coverage in which the employer pays the entire premium, no credit can be taken.

Planning Opportunity

Employers who agree to pay all or a portion of an employee's COBRA premiums for a period of time following an employee's involuntary termination should consider the impact of the

subsidy, and may wish to redesign existing plans. As noted, the federal subsidy is not available for any COBRA period in which the employer pays the entire premium. And the subsidy is reduced if the employer pays a portion (i.e., the AEI cannot be required to pay more than 35 percent of the amount not paid by the employer). Employers can reduce severance costs by eliminating (or reducing) employer-paid COBRA benefits.

Special Enrollment Option

Under COBRA, an employer may limit an AEI's COBRA option to the coverage option in which the qualified beneficiary was enrolled on the day before the qualifying event.

Under the Act, a group health plan is permitted to offer AEIs the opportunity to elect coverage under one or more group health plan coverage options that are different from the coverage in which they were enrolled on the day before the qualifying event.

The alternative coverage must be available under the plan generally (i.e., an employer cannot create alternative coverage for the assistance-eligible group only). In addition, the alternative coverage may not have a premium that exceeds the premium for the coverage in which the individual was enrolled at the time of the qualifying event. Furthermore, the alternative coverage cannot be coverage that provides only dental, vision, counseling, or referral services (or a combination of the foregoing); a health flexible spending arrangement; or coverage for treatment that is furnished in an on-site medical facility maintained by the employer and that consists primarily of first-aid services prevention and wellness care, or similar care (or a combination of such care).

Employers who choose to make this option available must provide notice of the option to AEIs (and potential AEIs) on or before April 18, 2009. An AEI (or potential AEI) has 90 days after the notice is provided to elect alternative coverage.

Preparing for Compliance

1) Assemble a Compliance Team

For many employers, compliance will involve an employer's human resources, payroll, and benefits personnel. Necessary outside parties will include third-party administrators, insurance companies (including stop-loss carriers for self-insured plans), and legal counsel. For example, an employer's COBRA administrator may need to make systems changes to accommodate the new notices and the special enrollment option (if offered by the plan).

2) Develop Guidelines for Determining When a Termination Is Involuntary

Currently, there is no formal guidance as to the meaning of “involuntary” for purposes of subsidy entitlement. Therefore, pending guidance, plans should develop guidelines, document them, and apply them uniformly.

The requirement that a termination be involuntary will raise a number of interesting questions, including the following:

- If an employee agrees to work on a temporary basis, is there an involuntary termination of employment when his or her employment ends?
- If an employee accepts an incentive package program because he or she is worried about impending layoffs, is the decision to leave employment voluntary?
- Suppose an employee chooses to quit because of an adverse development in his/her employment status (e.g., a decrease in pay; a diminution in authority, duties, or responsibility; a significant change in the geography where the employee is required to work, etc.). Is this truly voluntary?
- When an employee fails to return from FMLA leave and is subsequently terminated, is the termination involuntary?

3) Prepare a “Special Enrollment Notice” (Optional)

Will the plan implement the special enrollment option? As discussed above, the Act allows an employer to permit AEs to elect a less costly major medical plan as an alternative to the plan in which the individual was enrolled on the date before the qualifying event occurred.

4) Prepare a “Premium Reduction Notice” (Required)

This notice must be furnished to all qualified beneficiaries (not just qualified beneficiaries who are AEs or potential AEs) who become entitled to elect COBRA for any reason during the period beginning September 1, 2008 and ending December 31, 2009. As an alternative, the Act permits the plan to provide notice through a separate document furnished with the plan’s normal election notice. The Act directs the Secretary of Labor (DO”) or Secretary of Health and Human Services (HHS), as applicable, to publish a model notice not later than March 18, 2009.

Premium Reduction Notices Must Include:

- Any forms necessary for establishing eligibility for the premium reduction (e.g., attestation of subsidy eligibility)
- The name, address, and telephone number necessary

to contact the plan administrator and any other person maintaining relevant information in connection with the premium reduction

- A description of the extended enrollment opportunity
- A description of the qualified beneficiary’s obligation to notify the plan administrator of eligibility for coverage under a group health plan or Medicare and the penalty for failing to do so
- A description, displayed in a prominent manner, of the qualified beneficiary’s right to a reduced premium and any conditions on entitlement to the reduced premium
- If applicable, information and election forms with respect to the additional (less costly) coverage options an AEI may elect as an alternative to the coverage that must be offered

Premium Reduction Notices Should Include:

- A description of the qualified beneficiary’s right to expedited review (by DOL or HHS, as applicable) of denial of treatment as an AEI
- An explanation of the rights/obligations of high income individuals, and forms and instructions necessary to waive the subsidy up-front
- Information about how electing COBRA during the extended election period can help prevent (or reduce) the application of certain pre-existing condition exclusions

5) Develop an “Extended Election Period Notice” (Required)

This notice must be furnished by April 18, 2009. The Act directs the DOL and HHS, as applicable, to publish model notices not later than March 18, 2009.

6) Amend Group Health Plan Summary Plan Descriptions (SPDs)

7) Amend the Plan’s HIPAA Certificate of Creditable Coverage

For those who elect coverage through the special election period, any gap in coverage arising prior to February 17, 2009 is not considered a break in coverage for purposes of HIPAA’s creditable coverage rules.

Implementation Steps by Category of Qualified Beneficiary

1) Qualified Beneficiaries Who Experienced a Qualifying Event on or After September 1, 2008 and Had a COBRA Election in Effect on February 17, 2009

With respect to each individual who is not an AEI:

- Provide a Premium Reduction Notice on or before April 18, 2009

With respect to each AEI:

- Provide the Premium Reduction Notice on or before April 18, 2009
- Provide the Special Enrollment Notice on or before April 18, 2009 (if applicable)
- Obtain a written certification from the individual that he or she is not eligible for other group health plan coverage or Medicare
- Apply the subsidy to COBRA premiums for periods of coverage on or after February 17, 2009. For plans with monthly periods of coverage, the first period to which the subsidy could apply is March 1, 2009
- If the AEI pays an unsubsidized premium for March and April, establish and communicate a procedure for ensuring that the AEI is reimbursed for the excess amount paid⁴

2) Qualified Beneficiaries Who Experienced a Qualifying Event on or After September 1, 2008 and Before February 17, 2009 but Who Did Not Have a COBRA Election in Effect on February 17, 2009.

With respect to each individual who is not a potential AEI:

- Provide the Premium Reduction Notice

With respect to each potential AEI:

- Determine the COBRA coverage period. COBRA coverage (if elected) will begin on March 1, 2009 and end on the date it would have ended if COBRA had been elected at the time of qualifying event
- Provide the Extended Election Notice
- Provide the Premium Reduction Notice
- Provide the Special Enrollment Notice (if applicable)
- Obtain a written certification from the individual that he or she is not eligible for other group health plan coverage or Medicare
- Apply the subsidy to COBRA premiums for periods of coverage on or after February 17, 2009

Important Deadline: All notices to potential AEIs must be provided on or before Saturday, April 18, 2009.

3) Qualified Beneficiaries Who Experience a Qualifying Event on or After February 17, 2009 and Before December 31, 2009

With respect all qualified beneficiaries:

- Provide the Premium Reduction Notice with (or as part of) the COBRA election notice

With respect to potential AEIs:

- Provide the Special Enrollment Notice with (or as part of) the COBRA election notice (if applicable)
- Obtain a written certification that the employee is not eligible for other group health plan coverage or Medicare

Administrative Procedures and Business Records

1) Establish and communicate a procedure for ensuring that COBRA billings for periods of coverage for which the subsidy applies do not require payment of more than 35 percent of the applicable premium

2) Establish a procedure to ensure that the subsidy ends when an individual is no longer eligible to receive it

3) Keep careful business records relating to the following:

- The individuals to whom notices were furnished, and when, how, and by whom they were furnished
- Proof of each AEI's eligibility for COBRA at any time during the applicable period and election of COBRA coverage
- In the case of an insured plan, a copy of the invoice or other supporting documentation from the insurance carrier and proof of timely payment of the full premium to the insurance carrier required under COBRA
- In the case of a self-insured plan, proof of the premium amount and proof of the coverage provided to the AEI
- The amount of the subsidy reimbursed with respect to each covered employee and the covered employee's social security number, whether the subsidy was for single coverage or coverage for more than one person
- Attestation of involuntary termination for each covered employee whose involuntary termination is the basis for eligibility of the subsidy, including the date of the involuntary termination and the reason
- Information on the receipt, including dates and amounts, of the assistance eligible individuals' 35 percent share
- Any other document necessary to verify the correct amount of the reimbursement

¹ This Alert addresses the relationship between the Act and federal COBRA. Under the Act, continuation coverage that qualifies for the subsidy is not limited to federal COBRA; continuation coverage required under state law also qualifies for the subsidy. For example, medical plans maintained by private sector employers in New York with fewer than 20 employees would be covered by New York's "mini-COBRA" statute.

² For fully insured small plans that are subject to state law COBRA, the insurance carrier is entitled to recoup the portion of the premium that is not paid by the AEI.

³ The required payment can be as much as 150 percent of the applicable premium for disabled qualified beneficiaries receiving the 11-month disability extension.

⁴ As a general rule, the employer will reimburse the individual for the amount of the premium that exceeds 35 percent of the total premium or provide a credit for this amount that reduces one or more premium payments. If the credit method is used, the credit must be used within 180 days. If at any time during the 180-day period, it is reasonable to believe that the credit will not be used, payment equal to the remaining credit must be made within 60 days.

For more information, please contact:

Peter K. Bradley
pbradley@hodgsonruss.com

Anita Costello Greer
anita_greer@hodgsonruss.com

Michael J. Flanagan
mflanagan@hodgsonruss.com

Richard W. Kaiser
rkaiser@hodgsonruss.com

Arthur A. Marrapese, III
Art_Marrapese@hodgsonruss.com

Daniel R. Sharpe
dsharpe@hodgsonruss.com