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Changes to COBRA Under the American Recovery and Reinvestment Act of 2009 (ARRA): An Executive Summary and Outline for Employers¹

Introduction and Summary

On February 17, 2009, President Obama signed into law The American Recovery and Reinvestment Act (ARRA). ARRA provides for a 65% reduction in COBRA premiums, for up to nine months, for individuals who lost coverage due to an involuntary termination (for other than gross misconduct) occurring between September 1, 2008 and December 31, 2009. The 65% "subsidy" is paid for by the employer (or other entity to which premiums are payable), and then reimbursed by means of an offset against payroll taxes. The Department of Labor is in the process of preparing a model notice, which employers will be required to send to eligible individuals by April 18, 2009. The subsidy applies to premiums for months of coverage beginning March 1, 2009, but employers can continue to collect the full premium for another 60 days while they gear up, provided the overpayment can be applied against future premiums or is reimbursed.

The Department of Labor has created a new web page entitled *COBRA Continuation Coverage Assistance Under The American Recovery And Reinvestment Act Of 2009* with handy links to posters, fact sheets, flyers, FAQ's and other valuable information: <http://www.dol.gov/ebsa/COBRA.html> The IRS has also created a new informational web page entitled *COBRA Health Insurance Continuation Premium Subsidy*, containing links to the updated Form 941, Employer's Quarterly Federal Tax Return, and instructions: <http://www.irs.gov/newsroom/article/0,,id=204505,00.html> Links to both of these pages are on our website: www.hrwlawyers.com

Employers are encouraged to take the following steps now: (1) review the DOL and IRS web pages for further information, (2) determine if there are any individuals who are eligible for the subsidy (e.g., employees terminated for reasons other than gross misconduct after September 1, 2008); and (3) coordinate with their COBRA plan administrators and payroll and tax professionals regarding compliance with the new regulations, including whether/how to alert eligible individuals pending the DOL model notice, and arrangements for payment of the subsidy.

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Summary of Existing COBRA Requirements

- Group health plans must offer qualified beneficiaries the opportunity for continuation coverage after the occurrence of certain qualifying events.
- Qualifying Events include death, termination or reduction in hours for reasons other than gross misconduct, divorce or legal separation, a dependent child ceases to be a dependent or bankruptcy of the employer.
- Continuation coverage must be identical to the coverage provided under the plan to similarly-situated non-COBRA beneficiaries.
- For terminations, the minimum period is 18 months from the date of the qualifying event. Beneficiaries have 60 days from the date of notice to elect COBRA. They have 45 days after election to make their first premium payment, and a 30 day grace period for subsequent premium payments. The premium cannot exceed 102% of the applicable premium.
- COBRA imposes strict notice requirements, including a general notice at the time of enrollment and notice of COBRA continuation rights following a qualifying event.
- COBRA applies to employers with 20 or more employees. Many states, including Massachusetts, have "mini-COBRA" laws that impose similar requirements on smaller employers (in Massachusetts, 2-19 employees).

New COBRA Requirements Under the American Recovery and Reinvestment Act of 2009 (AARA)

Date Enacted: AARA was signed into law on February 19, 2009.

The 65% Subsidy:

- For a period not exceeding nine months, assistance eligible individuals are treated as having paid their full required COBRA premium if they pay 35% of the premium (i.e., 35% of the 102%).
- The subsidy is excludable from gross income for tax purposes, and also is not considered as a resource when determining eligibility for state or federal public assistance benefits.
- The subsidy also applies to coverage continuation through a state mini-COBRA law.
- The subsidy does not apply to contributions to a health flexible spending account.

- If a person “other than the individual’s employer” pays the 35% (e.g, a parent, guardian, state agency or charity), the individual is still treated as eligible for the subsidy.

Who it applies to: The subsidy applies to qualified beneficiaries (employees and their spouses/dependents) who elect COBRA and:

- the qualifying event was the loss of group health coverage on account of an involuntary termination (other than for gross misconduct), and
- the qualifying event occurs between September 1, 2008 and December 31, 2009.

Income Thresholds for the Subsidy – The “Recapture Tax”:

- If the individual’s modified adjusted gross income for the tax year in which the subsidy is received (either 2009 or 2010) exceeds \$145,000 (or \$290,000 for joint filers), the subsidy must be repaid in the form of an increase in income tax liability.
- If modified adjusted gross income is between \$125,000 and \$145,000 (\$250,000 and \$290,000 for joint filers), the amount that must be repaid is reduced proportionately.
- High net worth individuals can make a permanent election to waive the right to the premium subsidy.

Termination of the Subsidy: Eligibility for the subsidy terminates on the earlier of:

- nine months after the first month of coverage;
- at the end of the maximum applicable COBRA or mini-COBRA period; or
- when the individual becomes eligible for coverage under Medicare or another group health plan.
 - The individual is required to give written notice to the group health plan if he/she becomes eligible under another plan, or face a penalty of 110% of the subsidy.
 - Since the subsidy does not get reimbursed until after receipt of the 35%, the individual can avoid the penalty simply by ceasing to pay the 35%.

Option to switch to another plan: Group health plans are permitted (but not required) to provide individuals the option of switching to a lower-premium group health plan.

- This option does not apply to plans which only offer dental, vision, counseling or referral services, health flexible spending accounts, health reimbursement arrangements or on-site wellness facilities.
- If the individual switches, he/she can continue coverage under the new plan for the applicable COBRA period even after the nine month subsidy ends.

Special Election Period:

- There is a special election period of 60 days after notice is provided of the right to elect.
- Persons losing coverage on account of a termination between September 1, 2008 and December 31, 2009 must be given notice and an opportunity to elect, even if they did not elect before, or even if they elected in the past but lost coverage due to a failure to pay premiums.
- The special election period does not apply to coverage sponsored by employers with fewer than 20 employees that is subject to a state mini-COBRA law.

Rules applicable to people who take advantage of the special election period (i.e., persons who lose coverage on account of a termination between September 1, 2008 and February 19, 2009):

- The subsidy and coverage do not begin until the date of enactment (i.e., if the employee was terminated in September 2008, the coverage and subsidy still do not begin until March 1, 2009).
- The applicable COBRA period (usually, 18 months after the qualifying event) is not extended.
- If someone elects during the special election period, the period between the qualifying event and the enactment date must be disregarded for purposes of pre-existing condition limitations.

Reimbursement of the subsidy:

- The entity to which premiums are payable shall be reimbursed for the subsidy by means of a credit against liability for payroll taxes (income withholding plus FICA).
- If the amount of the subsidy exceeds the amount of payroll tax liability, the Secretary of the Treasury must reimburse the entity directly. This reimbursement is treated as a tax refund.

- The reimbursement also applies to subsidies made under state mini-COBRA laws.
- An entity is not eligible for reimbursement until the entity has actually received the reduced premium payment (i.e., the 35%).
- The Secretary of the Treasury can impose reporting requirements, including an attestation of the involuntary termination of the covered employee during the applicable period, the amount of payroll taxes offset and estimated offsets for the next reporting period.
- The IRS has issued a new Form 941, Employer's Quarterly Federal Tax Return, containing sections to report the dollar value of COBRA premium assistance payments and number of individuals provided COBRA premium assistance.

Notice requirements:

- The plan administrator must give the regular COBRA notice, plus notice of the new rights (availability of the subsidy, conditions for getting it, notification obligations, etc.).
- The new notice must be provided by April 18, 2009.
- The Department of Labor will issue a model notice by March 19, 2009.
- Plan administrators must provide notice about the premium reduction to individuals who have a COBRA qualifying event during the period September 1, 2008 – December 31, 2009. Plan Administrators may provide notices separately or along with the regular COBRA Notice.
- Notice must be provided to all individuals who terminated employment during the applicable time period, not just individuals who were involuntarily terminated.

Expedited Review: If an individual is denied COBRA (for example, because he/she was terminated for gross misconduct), the Department of Labor or the Department of Health and Human Services (in consultation with the Department of the Treasury) must provide an expedited review within 15 business days.

Regulations and Reporting: The Secretary of The Treasury is empowered to issue regulations or other guidance on the new law, including reporting requirements and provisions to prevent fraud. The Secretary of the Treasury must also issue interim and final reports to Congress regarding implementation of the law.

Effective Date:

- The law is effective for premiums for months (or shorter periods) of coverage beginning on or after the date of enactment. For plans that provide and charge COBRA continuation on a calendar month basis, the law is effective for the first calendar month following enactment (for most plans, March 1, 2009).
- A group health plan can continue to accept 100% of the premiums for two months (i.e., 60 days from the day of the first month after enactment date).
 - The entity accepting the premium may provide a credit to the individual against future premiums subject to the 35% rule, but only if it is reasonable to believe that the credit will be used within 180 days.
 - Otherwise, the entity must pay back the excess premium within 60 days.

What Employers Need to do Now

- Visit the Department of Labor's new web page entitled *COBRA Continuation Coverage Assistance Under The American Recovery And Reinvestment Act Of 2009* for handy links to posters, fact sheets, flyers, FAQ's and other valuable information: <http://www.dol.gov/ebsa/COBRA.html>
- Visit the IRS' new web page entitled *COBRA Health Insurance Continuation Premium Subsidy* for links to the updated Form 941, Employer's Quarterly Federal Tax Return, and instructions: <http://www.irs.gov/newsroom/article/0,,id=204505,00.html>
- Determine whether there are any individuals who are eligible for the subsidy (e.g., employees terminated for other than gross misconduct after September 1, 2008).
- Coordinate with plan administrators and payroll and tax professionals regarding compliance with the new requirements, including:
 - decide whether to give notice to these individuals now, or wait for the Department of Labor to issue a model notice; and
 - decide whether to start the subsidy right away, or continue to accept 100% of the premiums for some period of time while ramping up.