



# Legislative Update

February 26, 2009

## ARRA'S IMPACT ON COBRA

The American Recovery and Reinvestment Act of 2009 (ARRA) was signed into law by President Barack Obama on February 17, 2009. Although the provisions within the Act were effective with the President's signing, there are still many components of the law that require additional guidance. It is expected that the Department of Labor (DOL), the Treasury Department, and the Department of Health and Human Services (HHS) will provide regulatory explanations and model notices in the coming weeks.

While the ARRA covers a vast area of topics and encompasses several new laws, this legislative update will address the one area of the ARRA which significantly impacts employee benefit laws and administration; COBRA Continuation Coverage Assistance.

**New COBRA Law:** The ARRA introduces a new COBRA Continuation Coverage Assistance provision in which eligible individuals will be considered "paid in full" once the individual has paid 35% of the required COBRA premium for a "period of coverage" beginning on or after February 17, 2009. The Act defines a "period of coverage" as a monthly or shorter period of time with respect to which premium is charged.

Once the eligible individual's 35% of the charged amount is paid, the individual is entitled to receive a "subsidy" from the IRS for the remaining 65% of the premium. The 65% subsidy, according to the new COBRA laws must first be paid by the "person to whom premiums are payable under COBRA continuation" and will then be reimbursed by the IRS. Parties' eligible for subsidy reimbursement under the statute include employers and insurance companies (in certain circumstances when the state offers a "comparable" COBRA plan). In most cases, the employers, for both self insured and insured group health plans are required to pay the 65% subsidy.

The maximum period an individual may receive the COBRA subsidy is 9 months. The subsidy ends the earlier of 1) the date the qualified beneficiary is eligible (regardless of actual enrollment) for coverage under any other group health plan or 2) is eligible for Medicare. Eligibility for other group health coverage is not met if the other coverage offered under another group health plan is dental or vision only, counseling services or referral services. Additionally, the COBRA premium assistance must not last beyond the COBRA coverage normal expiration date.

---

Individuals who qualify to receive the subsidy will receive the premium reduction prospectively as of the date of enactment, February 17, 2009. The premium reduction may not be claimed retroactively.

**What about Small Businesses?** For states that offer continuation coverage to employees of small employers (with less than 20 employees), qualified individuals will be entitled to the subsidy if the state benefits are “comparable” to COBRA.

**Who Does This Apply To?** With the exception of health flexible spending accounts (FSA’s), all group health coverage noted under current COBRA provision and ERISA are covered under the Act. The new laws encompass medical coverage, dental, vision, and prescription drug coverage regardless of whether coverage is offered on a stand-alone or “bundled” basis. HSA’s and some EAP’s are also covered under the law.

**Eligibility Requirement for COBRA Coverage Assistance:** To qualify for the COBRA “subsidy” noted in the new laws, the following requirements must be met:

- Lost of coverage must be due to an involuntary termination of employment between September 1, 2008 and December 31, 2009 for the employee and/or eligible dependents (qualified beneficiaries) to qualify for the subsidy.
- The qualified beneficiary is eligible for COBRA and elects continuation coverage.

Individuals who meet the above requirements and are entitled to the COBRA assistance subsidy (premium reduction) are referred to as **“Assistance Eligible Individuals” (AEI)** under the new Act.

**COBRA Enrollment and the 60 Day Extended Open Enrollment Requirement:** All qualified beneficiaries who lost coverage since September 1, 2008 and did not elect COBRA at the time, **must** be provided an extended open enrollment period of 60 days. Even qualified beneficiaries whose qualifying event was not an involuntary termination of employment must be advised of the extended open enrollment. This also includes qualified beneficiaries who did not elect COBRA previously. Additionally, qualified beneficiaries who elected COBRA before the Act, but were no longer enrolled on the date of enactment (e.g. because of the inability to pay the COBRA premium), is also entitled to elect COBRA coverage during the extended election period.

The 60 day extended open enrollment period began on the date of the enactment, and ends 60 days after the date the notice regarding the extended election period was provided to the qualified beneficiary. Additional information regarding the employer’s notice requirements are discussed below.

---

---

COBRA coverage elected during the extended election period must:

- a) Begin on or after the date of enactment
- b) Not extend beyond the period of COBRA continuation coverage required if the coverage would have been elected under the standard election period.

For additional clarity, the extended election does not lengthen the period of COBRA continuation beyond the original maximum period; rather it provides qualified beneficiaries, including those eligible to receive the subsidy (AEI's), additional time to elect COBRA continuation coverage.

Notably, when participants elect coverage during the extended open enrollment period, health plans may not consider any break in coverage for the purposes of pre-existing condition exclusions.

**Income Tax Considerations/Tax Implications:** The 2009 Recovery Act does not impose income limits for AEI's receiving the COBRA subsidy, but the Act does have a premium assistance recapture provision which imposes a cap of \$145,000 modified adjustable gross income for individuals and \$290,00 for joint income earners. Generally, the recapture provision means that Individuals whose income exceeds the mentioned amounts in a given tax year and receives the subsidy during the same year, must account for the premium reduction when filing taxes and the taxpayer's income tax will be increased by the amount of the premium assistance. The subsidy is reduced for individual income earners with a modified adjustable gross income over \$125,000 (joint income earners over \$250,000) and these tax payers are subject to a graduated phase out calculation detailed in the Act.

Employers are not expected to monitor the income of qualified beneficiaries or AEI's to determine subsidy eligibility.

**Reimbursement for the Subsidy:** To be reimbursed for the subsidy employers are entitled to take a reduction in payroll taxes. The reduction to payroll taxes may not begin until the employer has received the AEI's 35% payment. The credit will be applied as though the employer had submitted an equivalent amount of payroll tax on the date the AEI's payment is received. In the cases where the amount paid by the employer exceeds the amount of the employer's liability for payroll taxes, the IRS will credit or refund the excess in the same manner as if it were an overpayment of payroll taxes. Consequently, any overstatement of the reimbursement which results in the IRS reimbursing for the overstatement will be treated as an underpayment of payroll taxes and may be collected by the IRS in the same manner as payroll taxes.

To allow employers to get acclimated with the new COBRA laws, the Act incorporates a special transition period which theoretically gives employers and insurers time to develop procedures for complying with the Provision. In the case of an AEI who pays more than the 35% charged amount during the first two coverage periods immediately following enactment, the employer must reimburse the AEI for the overpayment. The employer may make a reimbursement payment to the AEI for the amount overpaid, or the employer may provide a credit to the AEI for the amount that reduces subsequent premium payments the AEI is required to pay. Should the employer adopt the later

---

---

option, the employer must still reimburse the AEI within 60 days of the overpayment if it is believed the credit (overpayment) will not be used within 180 days.

Employers who have agreed to pay the entire COBRA premium for a qualified beneficiary as terms of a severance agreement or other arrangement is not eligible to take the subsidy. If the employer agrees to pay a portion of the COBRA premium, the employee will only be responsible for 35% of the required portion and the employer may take a tax credit for only the remaining 65% of the employee's portion.

**Example:** The full COBRA premium is \$1000 (including the administration fee) for an involuntarily terminated employee. The employer agrees to pay 80% of premium or \$800 as part of a severance agreement. The employee is responsible for \$200 or 20% of the COBRA premium as part of the arrangement. Assuming the employee is an AEI under the ARRA, the employee is now required to pay \$70 (35% of \$200). The employer may only take a payroll tax credit for \$130 (65% of the employee's \$200). The employer is not permitted to take a tax credit for the original \$800 the employer agreed to pay.

In the event that State continuation coverage is offered in lieu of COBRA (referring to the small employer COBRA exemption) the insurance carrier and not the employer will be entitled to the payroll tax credit, even though the credit does not cover the carrier's employees.

**Employer Notification Requirements:** Current COBRA provisions require plan administrators, following the qualifying event, within 14 days of being provided notice of the qualifying event, to provide each qualified beneficiary with a notice that explains the individual's right to elect COBRA, the coverage that may be elected, the duration of coverage, the cost of coverage and information regarding when premiums are due.

***Employers, under the Act, are required to send a new notice to all qualified beneficiaries who became entitled to COBRA continuation between September 1, 2008 and December 31, 2009.***

The American Recovery and Reinvestment Act of 2009 (ARRA) requires the additional notification to advise qualified beneficiaries of the availability of the subsidy, and provide a description of the option to enroll in different coverage if this is permitted by the employer. If notices fail to meet these criterions, the plan sponsor will be treated as not meeting COBRA notice requirements.

The new notice requirement may be met by modifying the existing COBRA notice to include the required information specified in the law or a separate document may be provided which meets the requirements. The additional notice must include:

1. Forms necessary to establish eligibility for premium reduction (subsidy)
  2. All contact information including name, address and telephone number for the plan administrator and any other person maintaining information in connection with the subsidy
-

3. A description of the extended election period
4. A description of the obligation of the qualified beneficiary to notify the plan providing COBRA when other coverage is available under another group health plan or Medicare. The consequences for the failure to notify the plan administrator when other coverage becomes available must also be noted.
5. A description of the qualified beneficiary's right to a reduced premium and any conditions on entitlement to a reduced premium, displayed in a prominent manner.
6. If the employer permits, a description of the option for the qualified beneficiary to enroll in a different coverage option than what was selected at the time coverage was lost.

As previously mentioned, this notice must be provided to all persons who become eligible for COBRA during the subsidy period and the plan administrator must within 60 days of the date of enactment, provide the notice to any qualified beneficiaries who had elected COBRA coverage as of the date of enactment. Individuals eligible to take advantage of the extended election period must also be given the additional notice.

The DOL, IRS, and HHS must issue models for the required additional notification within 30 days of the date of the enactment.

**The Option to Select Different Coverage:** Pre-Act COBRA rules required qualified beneficiaries to elect COBRA coverage identical to what was in place prior to the loss of coverage. Under the COBRA Assistance Provisions, AEI's may enroll in coverage that differs from the coverage in place prior to the qualifying event, should the employer permit. The different coverage must be coverage offered to active employees and can not be only dental, vision, referral or counseling services. Additional coverage options also exclude on-site medical facilities that provide first aid or wellness care. The premium of the optional coverage may not exceed the premium of the coverage the AEI was enrolled in prior to the qualifying event.

**Employer Reporting Requirements:** While we are still awaiting additional regulatory clarity from the IRS, the DOL and the HHS, the ARRA notes certain employer reporting requirements. While specific reporting formatting and due dates have yet to be determined, the Act outlines three types of reports employers will be required to provide to the DOL or the IRS. In the report(s) employers are expected to:

1. Prove that each qualified beneficiary who receives a subsidy was due to an involuntary termination.
2. Report the payroll tax credit taken for the reported period and estimate tax credits that will be taken for the following period.
3. Provide a detailed report on the all covered employees, the amount of the subsidy treated as a payroll tax credit for each employee and list if the subsidy is for one individual or two or more individuals.



**Employer's Action Steps toward Compliance:** We realize that complying with the requirements of a legislative change may be an overwhelming experience for our Clients. At Conner Strong, we are here to help you. To ensure that you are in compliance with this new law, it would be advisable to:

- Identify all subsidy eligible individuals (AEI's) including current and potential individuals.
- Prepare and send notices of the extended enrollment period to all qualified beneficiaries who lost coverage between September 1, 2008 and December 31, 2009. Be sure that notices include all required elements outlined in the Act.
- To meet reporting obligations, develop a system for tracking AEI's and the period AEI's are available for coverage.
- Review and update current plan notices, documents, and applicable forms. This may involve revising SPD's and issuing SMM' s to detail premium assistance rights, plan enrollment options, if offered, and the AEI obligation to notify the employer when other group health coverage or Medicare become available.
- Evaluate COBRA administrative practices to ensure they are compliant with the new laws.

**Please contact your Conner Strong representative with any questions, toll-free at 1-877-861-3220.**

*This Legislative Update is provided for general informational purposes only and is not intended to be legal advice. Readers are urged to contact an attorney for legal advice or assistance.*

