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eAlert

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## *BENEFITS NOTEBOOK*

### **STIMULUS BILL MANDATES COBRA CHANGES**

The stimulus bill, formally titled the American Recovery and Reinvestment Act of 2009, passed by the House and Senate last week and expected to be signed by President Obama *tomorrow*, includes two temporary but major changes to the rules regarding continuation coverage. (A larger and permanent change did **not** pass – it would have required health plans to extend the maximum continuation period to Medicare enrollment for “qualified beneficiaries” losing coverage due to termination of employment or reduction in hours after reaching age 55 or earning ten years of service.)

To review, the Consolidated Omnibus Budget Reconciliation Act of 1985 requires most employers’ group health plans (*public as well as private*, insured as well as self-insured) to permit current and former employees, spouses and dependents who lose their coverage due to the “qualifying event” of termination of employment or reduction in hours to continue their coverage for up to 18 months by continuing to pay the premium for coverage during the continuation period. “Group health plans” are defined broadly by COBRA to include not only medical plans but also dental, vision, prescription-drug, health flexible spending account, health reimbursement arrangement and certain wellness and employee assistance plans.

The two major exceptions to the COBRA continuation-coverage mandate apply to “church plans” and plans maintained by employers who normally employed fewer than 20 employees on a majority of their business days during the calendar year preceding the qualifying event. (Oregon-insured plans of small employers exempt from COBRA may be required by the Oregon Insurance Code to offer continuation coverage for up to six months.) The stimulus bill doesn’t change the rules regarding who may be eligible for federal or Oregon continuation coverage.

The two changes made by the stimulus bill relate to (1) the premium for continuation coverage and (2) opening a new window that would permit certain qualified beneficiaries who are *not* on COBRA coverage to elect such coverage.

## **Premium for Continuation Coverage**

The bill permits certain qualified beneficiaries to obtain continuation coverage by paying 35% of the “applicable premium” for such coverage. (The applicable premium is generally 102% of the cost of coverage for a similarly situated non-COBRA participant). For example, if the cost of employee-only coverage under a health plan were \$500 per month, the COBRA applicable premium might be \$510 per month, of which the qualified beneficiary (or someone else, other than the employer, on the qualified beneficiary’s behalf) would have to pay only \$178.50 per month (35% of \$510) to retain continuation coverage, subject to the special rules discussed below.

The stimulus bill provides that if the qualified beneficiary is eligible for the premium reduction discussed above, the employer is to pay the remainder of the continuation-coverage premium (\$331.50, in the example above) *and then take a credit against its obligation to withhold and remit federal income and FICA taxes from employees’ compensation and to pay the employer share of FICA taxes.* An employer whose continuation coverage subsidy is greater than its withholding and FICA obligations is entitled to a direct payment from the federal government for the shortfall.

Of course, there are restrictions on the premium subsidy, including the following:

- It applies only to qualified beneficiaries who lost or lose coverage due to involuntary termination of employment (subject to the gross-misconduct exception, if the plan uses that exception) between September 1, 2008 and December 31, 2009 (so it may reduce future COBRA premiums for qualified beneficiaries already on continuation coverage). It appears that loss of coverage due to death or reduction in hours does not trigger the subsidy.
- The premium subsidy first applies to periods of coverage starting after the date President Obama signs the bill (so for March 2009 coverage, in most cases).
- The premium subsidy is available for up to nine months, but it doesn’t extend the COBRA continuation period, and the subsidy ends when the qualified beneficiary becomes *eligible for* (not necessarily covered by) Medicare or by another group health plan (other than a plan providing only ancillary coverage – dental or vision only – or a health FSA) or fails timely to pay his or her reduced share of the applicable premium. The subsidy may last beyond 2009, if the termination occurred during the relevant period. The qualified beneficiary is required to give notice in writing to the plan administrator of eligibility for other group coverage and may be subject to a penalty for failure to do so.
- The group health plan is obligated to decide whether the qualified beneficiary is eligible for the subsidy (including whether the termination was involuntary), subject to expedited review by the U.S. Department of Labor of any denial of eligibility.
- The premium subsidy is even available for *non-COBRA* continuation coverage attributable to an involuntary termination of employment during the relevant period, such as Oregon’s six-month continuation for Oregon-insured small-employer plans and our super-continuation rights for early retirees from Oregon public employers.
- The subsidy is available for COBRA coverage under health plans other than basic medical plans, but not health FSAs. So if the employee were covered by medical, dental and vision plans, with a combined premium for active employee-only coverage of \$600 per month and a

COBRA applicable premium of \$612 per month, an eligible qualified beneficiary could continue all three coverages for March 2009 and thereafter by paying \$214.20 per month.

- The employer is permitted, but not required, to offer eligible qualified beneficiaries a 90-day window in which to elect to continue coverage in a different, less expensive group health plan that is not a health FSA or a plan providing only ancillary coverages.
- The employer obtains reimbursement for its payment of the remainder of the continuation-coverage premium when it submits IRS Form 941 for discounted premiums it receives from eligible qualified beneficiaries, apparently regardless of when the employer makes up the difference between the qualified beneficiary's payment and the full applicable premium.
- The subsidy is not available if the employer pays the qualified beneficiary's share of the applicable premium.
- The subsidy is not taxable income to the qualified beneficiary or reportable as such by the employer, nor is the subsidy income for purposes of entitlement to public benefits.
- The premium subsidy is available to each affected qualified beneficiary and not limited to the terminated employee, nor is it dependent on the terminated employee electing or retaining continuation coverage.
- A qualified beneficiary with adjusted gross income above \$125,000 (\$250,000 for joint filers) for a year in which the beneficiary receives a premium subsidy is subject to an additional tax to recoup the subsidy. The tax is phased in between \$125,000 and \$145,000 of adjusted gross income (\$250,000 - \$290,000 for joint filers).
- Plan administrators must give eligible qualified beneficiaries notice of the availability of the premium subsidy, as well as the requirement that qualified beneficiaries give timely written notice of the availability of other coverage that may cut off the premium subsidy. The notice must include the forms necessary to establish eligibility for the premium subsidy and the name, address and telephone number of the plan's contact person

### **Special Window for COBRA Enrollment**

Group health plans subject to COBRA must offer a new or extended election window to qualified beneficiaries described above (who lost coverage due to involuntary termination on or after September 1, 2008) but who either did not timely elect COBRA continuation coverage or who dropped such coverage. Of course, this requirement, too, is subject to technical rules:

- Plan administrators must give eligible individuals notice of the new or extended election window, which must last 60 days from the date of the notice. (So a qualified beneficiary, Ann, whose employment was involuntarily terminated in September 2008 and did not elect COBRA coverage, would have to be offered such coverage again, and the election period for a qualified beneficiary whose employment was involuntarily terminated in December 2008 and has not yet elected COBRA coverage would have to be extended.) The DOL is to prepare a model notice.
- COBRA coverage elected during the special election period begins on the first coverage period after President Obama signs the bill (presumably March 2009) and does not extend the maximum COBRA continuation period based on the original qualifying event. (So the

maximum COBRA continuation period for qualified beneficiary Ann, described above, would normally end on February 28, 2010, though Ann did not have continuation coverage from October 2008 through February 2009.

- If a qualified beneficiary elects COBRA coverage during the special election period, any gap in coverage between the date of the qualifying event and March 1, 2009 is disregarded for purposes of applying any preexisting-condition limit to the qualified beneficiary.
- The special election period, unlike the premium subsidy, appears to apply only to COBRA coverage and not to other forms of continuation coverage, such as state-mandated coverage.

### **Employer Action Steps**

Employers will want to move quickly to address the continuation-coverage changes made by the stimulus bill. We suggest the following steps:

- Consider whether to offer eligible qualified beneficiaries alternate continuation coverage under a plan less expensive than the actual COBRA plan.
- Prepare and circulate notices announcing the premium subsidy (and providing the related information described above).
- Identify the qualified beneficiaries eligible for the special election window and prepare and circulate a notice offering them COBRA coverage, including the premium subsidy.
- *Consider how the premium subsidy might facilitate separation agreements or reductions in force and whether severance pay plans should be amended, since employer-subsidized continuation coverage is not eligible for the subsidy.*
- Self-insured employers might revisit their determination of the COBRA applicable premium, since the premium subsidy is likely to increase IRS scrutiny of the applicable premium.
- Employers' benefits and payroll professionals will want to coordinate to ensure the employer gets timely credit against its federal payroll taxes for its subsidized COBRA premiums.

Please feel free to contact us if you have questions or comments about these new rules, or any matters relating to employer-sponsored benefits.

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~EMILY Q. SHULTS  
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