

The American Recovery and Reinvestment Act (ARRA) of 2009 and the Impact on COBRA Guide

Overview

As of February 17, 2009, the American Recovery and Reinvestment Act (ARRA) addresses the amendments to the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) that will affect every employer that sponsors a group health plan for employees and has terminated or laid off an employee on or after September 1, 2008.

These amendments create additional COBRA notice requirements and affect payroll tax administration in order to administer a temporary federal subsidy of COBRA premiums. Employers need to implement the new requirements immediately and are expected to locate former employees (if impacted) and coordinate with payroll and COBRA administration departments. The Act also requires the Department of Labor (DOL) to provide outreach, focusing on employers and others, consisting of education and enrollment assistance that will first target those individuals terminated from employment prior to enactment of the Act.

Federal Subsidy Defined

Under the ARRA, for COBRA coverage periods beginning on or after February 17, 2009, "assistance eligible individuals" will be required to pay 35% of the applicable COBRA premium. Employers that provide group health coverage through insurance will need to cover the remaining 65% of the premiums until reimbursement can be requested from the federal government. Employers that provide coverage through insurance or self-insurance will be able to obtain reimbursement of the 65% premium subsidy as a credit against their quarterly federal employment tax filings. The subsidy applies regardless of the level of coverage (single, single plus one, family, etc.).

Affected Businesses

In general, COBRA does not apply to small health plans where the employer sponsoring the plan has fewer than 20 employees. In some states, these plans are subject to state (or "mini-COBRA") statutes that mandate various levels of continuation coverage. However, the subsidy would be available with respect to such plans where the state continuation coverage requirements are comparable to the continuation coverage requirements under COBRA.

Subsidy Time Duration

While available for up to nine (9) months, the subsidy can end sooner, such as when the maximum continuation coverage period under COBRA expires. (Note: The statute does not extend the maximum COBRA continuation coverage periods.) Additionally, the subsidy will stop being available for COBRA coverage following the date an assistance eligible individual becomes eligible for:

1. Coverage under any other group health plan (other than one consisting only of dental, vision, counseling or referral services);
2. Coverage under a health flexible spending account plan;
3. Coverage of treatment at certain employer on-site facilities; or
4. Medicare or Medicaid.

Employer Notifications of Changes

The DOL specifies the time and manner of notice. Under the ARRA, absent reasonable cause and willful neglect, the failure to provide notification changes would subject the individual to a penalty equal to 110% of the premium reduction provided after termination of eligibility.

Assistance Availability for Eligible Individuals

“Assistance Eligible Individuals” (AEIs) under the Act are individuals who:

1. Are or were otherwise eligible for COBRA continuation coverage,
2. Lost coverage under their employer-sponsored group health plan due to an involuntary termination of employment between September 1, 2008 and December 31, 2009, and
3. Elect COBRA continuation coverage.

While the Act does not expand on what constitutes an involuntary termination, any type of involuntary termination qualifies for the subsidy, including an involuntary termination for cause unless it amounts to a COBRA gross misconduct situation.

The ARRA does require the DOL to provide expedited review of any situations where an individual requests treatment as an AEI and the group health plan denies that treatment. Under this provision, the DOL is required to make its determination within fifteen (15) business days of the date it receives the individual's application for review.

Candidates Declining COBRA prior to ARRA Provisions

Some individuals who were recently terminated may have declined to elect COBRA continuation coverage because of its cost. The ARRA includes a special election opportunity for AEIs who were eligible to elect COBRA coverage when they were terminated from employment but did not choose to elect. These individuals are entitled to an extended election period that begins on February 17, 2009, and ends no sooner than sixty (60) days after an extended election notice is provided to the individuals. *It is important to note that this extended election period does not change the fact that the individual's termination from employment remains the qualifying event for purposes of COBRA.*

The ARRA requires employers to locate former employees who previously declined COBRA and provide notice of the right to COBRA coverage with the government subsidy. If an eligible individual elects COBRA continuation coverage during the special extended election period, COBRA coverage will commence with the first period of coverage beginning on or after February 17, 2009. However, for purposes of determining the maximum COBRA coverage period, the date of the individual's involuntary termination of employment (or the date of the loss of coverage resulting from such termination, if applicable) will continue to be treated as the “qualifying event.” This means that the COBRA continuation coverage period available to an individual who makes an election during the extended election period will be determined based on the date of the qualifying event as described above.

- *Example:* An AEI terminated on September 30, 2008, who makes a timely election during the extended election period, generally will be entitled to COBRA continuation coverage prospectively beginning March 1, 2009, though the 18-month maximum coverage period is measured from October 1, 2008.

Candidates Paying Full COBRA premium

The ARRA entitles assistance to eligible individuals for reimbursement from the employer for the excess over which the individual is required to pay under the ARRA or a credit of that amount against future COBRA premium payments. The credit is permissible depending on whether it is reasonable to expect the individual to use it within 180 days of the full premium payment.

Enrollment Plan Options

Under COBRA, a qualified beneficiary generally is entitled only to elect continuation of the same coverage option he or she was receiving on the day before the date of the qualifying event. The ARRA does allow employers for some flexibility. Assuming different coverage options are available, an AEI may enroll in coverage under a plan that is different than the coverage in which he or she was enrolled at the time the qualifying event occurred. To make this change, the AEI must make his or her election change within ninety (90) days after receiving notice. Such election must be permitted by the employer. The premium for such coverage must not exceed the premium for the coverage in which the individual was enrolled prior to termination of employment. In addition, the different coverage also must be offered to active employees at the time the election is made and the different coverage may not be coverage providing only dental, vision, counseling, referral services (or a combination of these), coverage under a flexible spending arrangement, or coverage that provides services at certain on-site medical facilities.

Income Limitations and Impacts

AEIs who receive a subsidy under the ARRA and who are considered high-income individuals will see their income tax liability increased by the amount of the subsidy for the tax year in which they receive the subsidy. High-income individuals are those individuals with modified adjusted gross income (AGI) that exceeds \$125,000 (\$250,000 in the case of joint return filers) for the tax year in which they receive the subsidy.

Employer Notice Requirements

Employers will need to amend their current COBRA election notices temporarily to include general information about the availability of the premium subsidy and, if applicable, the option to enroll in different coverage. Specifically, the notices must include:

1. The forms necessary for establishing eligibility for the premium subsidy;
2. Contact information of the plan administrator and any other person with information regarding the premium subsidy;
3. A description of the extended election opportunity for those who previously declined COBRA continuation coverage;
4. A description of an AEI's obligation to notify the plan when he or she becomes eligible for coverage that would cause eligibility for the subsidy to cease and the penalty for the failure to do so;
5. A prominent description of the qualified beneficiary's right to the COBRA subsidy and any conditions on such right; and
6. A description of the option to enroll in different coverage under the health plan, if applicable.

This information must be included in the COBRA election notices provided to persons who become eligible for COBRA continuation coverage after February 17, 2009. For AEIs who became eligible for COBRA continuation coverage prior to February 17, 2009, a similar notice must be provided within sixty (60) days of February 17, 2009.

Employer Steps to Apply for Reimbursement

Since the federal COBRA premium subsidy is reimbursed to employers through the federal quarterly payroll tax reporting system, the ARRA requires employers to advance the premium subsidies until the employer's payments can be recouped through reduced federal payroll tax payments. Employers will have to determine the total amount of the subsidy with respect to premiums received during the federal payroll tax reporting period from assistance eligible individuals that have elected COBRA continuation coverage. The employer may use this amount as an offset to its federal payroll tax liability. For purposes of the Act, "payroll taxes" include amounts to be withheld for federal income taxes and the employer and employee portions of FICA Social Security and Medicare taxes.

To the extent that such amount exceeds that of the employer's liability for these federal payroll taxes, the Internal Revenue Service (IRS) will reimburse the employer for the excess directly. If an employer claims too much in reimbursement, it will be treated as an underpayment of federal payroll taxes to be assessed and collected accordingly.

In addition to expected modifications to current payroll tax reporting forms, the ARRA requires additional information be provided by employers seeking reimbursement of subsidy payments, such as attestations of involuntary terminations and of coverage levels individuals are receiving.

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Frequently Asked Questions (FAQs)

1) What is the purpose of the new COBRA provisions in the American Recovery and Reinvestment Act?

To assist group health plan participants who have lost or will have lost their jobs between the dates of September 1, 2008 and December 31, 2009 with the payment of their COBRA premiums.

2) How do the new provisions assist group health plans?

Generally, the new provisions allow these people to fulfill their monthly COBRA payment obligation by paying only 35% of their COBRA premium for a nine (9) month period. The federal government intends to subsidize the other 65% of the premium amount through credits against the employer's payroll tax liability. The government has budgeted almost \$27 billion for the subsidy.

3) Which employers do the new COBRA provisions affect?

All employers that are subject to COBRA are subject to these provisions, including state and local employers covered under the continuation rules of the Public Service Health Act and plans sponsored by the federal government.

4) When are the new provisions effective?

The new provisions apply to premiums for a period of coverage beginning on or after the date of February 17, 2009. Since most insurance contracts run on periods of coverage tied to calendar months, in most cases, the new provisions will apply to COBRA premiums for periods of coverage beginning on March 1, 2009. The Act requires that appropriate notices be sent by April 18, 2009.

5) Do the new provisions change or replace other COBRA provisions?

No. All other COBRA provisions remain intact. Think of these new provisions as a sort of "add-on" to the original COBRA language as opposed to a replacement of that language. This subsidy is intended to be a temporary measure, though it will greatly disrupt the traditional administration of COBRA over the next two years or so.

6) Will the 65% subsidy increase COBRA participation?

Since the subsidy will lower the out-of-pocket cost for COBRA participants, this subsidy very likely will dramatically increase COBRA participation.

7) Who is eligible for the premium assistance?

An AEI is defined by the new provisions as any qualified beneficiary who at any time during the period of September 1, 2008 and December 31, 2009:

1. Is eligible for COBRA continuation coverage,
2. Elects such coverage, and
3. Lost coverage originally due to involuntary termination occurring during such period.

8) What about employees who were involuntarily terminated on September 1, 2008 or thereafter and have already declined or terminated COBRA coverage?

The new provisions allow former employees who would have been AEIs on the date of the bill's enactment (had they not already declined COBRA coverage) to jump back onto such coverage. Essentially, this means that former employees who have already declined or terminated COBRA coverage get a second chance to sign up for COBRA. For shorthand purposes, we call these "second-chance AEIs."

9) Are there any income limitations on the subsidy?

The subsidy does not apply to employees or dependents whose “modified adjusted gross income” (basically adjusted gross income increased by certain exclusions) is more than \$125,000 (\$250,000 for joint filers) for any year in which they would receive the subsidy. If any such “high-income earner” does receive the subsidy, their income tax liability will increase accordingly. High-income earners will have the right to waive the subsidy to avoid this liability. Furthermore, the actual tax liability has some “phase-in” provisions for certain such taxpayers. We expect further guidance from the Internal Revenue Service (IRS) on this subject in a very short time; however, at this moment, we do not expect that it will be the responsibility of the employer to determine whether income limitations apply.

10) Will the subsidized coverage extend the typical COBRA coverage time frame?

No. The nine-month period for the subsidized coverage is concurrent with the normal COBRA timeframe. It is not in addition to it. No AEI’s maximum COBRA period will be extended. “Second chance” AEIs will not get a retroactive subsidy; however, their original qualifying event date will remain their first day of COBRA for purposes of calculating the maximum period. Also, note that the subsidy will likely cause AEIs to remain on COBRA for longer than normal qualified beneficiaries.

11) Are there any other limitations on the subsidy, besides the nine (9) month period?

The subsidy period terminates when the AEI is eligible for coverage under another group health plan (not including dental plans, vision plans or other limited plans, and flexible spending arrangements) or Medicare. Under the law, it is the responsibility of the AEI to notify the plan administrator of this eligibility. If an AEI does not, he or she may be required to pay a penalty of 110% of the premium reduction unless the failure is due to “reasonable cause.”

12) Does the subsidy apply to COBRA coverage for health flexible spending arrangements (FSAs) and health reimbursement arrangements (HRAs)? What about “limited” insurance plans like dental or vision plans?

The law specifically exempts FSAs from its application, but does seem to include HRAs. It also applies to dental and vision insurance plans, as well as any other group health plans typically subject to COBRA. Since an HRA is simply a self-insured group health plan, to calculate the 65% subsidy for an HRA plan, a plan administrator would simply multiply the HRA COBRA premium by 65%.

13) How do potential AEIs who have already been terminated get notice of the subsidy?

The appropriate notices should be sent out as soon as administratively possible to begin the recipient's election period. While the IRS and the DOL are expected to issue further guidance, it's important to be mindful of the deadlines imposed by ARRA.

14) How is the subsidy going to be distributed?

The subsidy will take the form of a “tax subsidy,” meaning that the federal government will not be writing checks to employers or insurers. Rather, employers will be able to take the 65% of the monthly COBRA premiums paid on behalf of COBRA participants as a credit against their federal payroll tax liability. Essentially, the federal government is subsidizing the COBRA participant but having the employer do all of the work. We expect significant guidance on the actual procedures regarding this issue in the near future.

15) If the company subsidizes COBRA coverage for some terminated employees, can the employer recoup some of that money from the new required subsidy?

Unfortunately, it does not appear that companies which already subsidize COBRA coverage for terminated employees will be able to enjoy any recoupment of those funds from the new required subsidy.

16) How is the 2% COBRA administration fee accounted for in the subsidy?

The language of the bill does not expressly address this issue, so we will have to wait for further guidance. However, the general belief among industry observers is that the bill implicitly includes the 2% administration fee as part of the premium. We will have to wait and see what the agency guidance tells us.

17) Will the federal government play any role other than providing the subsidy and publishing guidance?

The law specifically mandates that the Department of Labor, the Department of the Treasury and the Department of Health and Human Services provide “outreach” to employers, plan administrators and so on. The clear purpose of this outreach is to promote the COBRA subsidy as much as possible. Moreover, the law calls for an “expedited review” by either the Department of Labor or the Treasury in cases of any former employee who is denied treatment as an AEI. We believe that the very active role taken by these federal agencies will result in cautious employers granting “AEI” status to terminated employees in all but the most certain cases of “voluntary” termination.

18) Are there any other provisions to be aware of?

The new law gives AEIs ninety (90) days to elect different and less expensive health coverage (excluding “limited” plans like dental, vision and health FSA plans) than they had at the time of their termination. However, this is only available if the employer wants to allow for such an option and if this optional coverage is also offered to active employees.

Employers wishing to allow AEIs to participate in this “AEI special enrollment” must be prepared to answer plan questions for potential AEIs, provide documentation (such as plan information, Summary Plan Descriptions, etc.) and keep track of enrollment periods.

Also, with regard to “second chance” AEIs (people who were terminated in the past and would be AEIs now except that they never elected or they dropped their COBRA coverage), the period of time between the termination and their first period of subsidized coverage is to be disregarded for purposes of calculating the 63-day “preexisting condition” rule under HIPAA.

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