

Employer Compliance Alert



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▶ Stimulus Package Includes 65% COBRA Premium Subsidy

Among the items included in the recent economic stimulus package (formally known as the American Recovery and Reinvestment Act) is a temporary subsidy of COBRA premiums for involuntarily terminated employees. Although the Act omits language from the House bill that would have mandated an extension of COBRA coverage through age 65, it does require employers and other plan sponsors to facilitate this federal subsidy of COBRA premiums. The subsidy will cover 65% of the monthly premium, for a period of up to nine months.

Eligibility for Subsidy

To qualify for this premium subsidy, an employee must be *involuntarily* terminated between September 1, 2008, and December 31, 2009. The subsidy will not apply to employees who voluntarily resign, nor to employees who lose their health coverage due to a reduction in work hours. Although the Act applies to employees who may have been terminated as long ago as September 1, 2008, the subsidy is not retroactive. It will apply only to periods of coverage (generally months) beginning on or after March 1, 2009.

This subsidy is available not only for COBRA coverage, but also for similar state-mandated continuation coverage. It is not available, however, for coverage under a health flexible spending arrangement.

The subsidy applies to whatever level of COBRA coverage the terminated employee elects – whether single-only, single-plus-one, or family. An employer may – but need not – allow an eligible employee to elect COBRA coverage under an option that differs from the employee’s pre-termination option, so long as the premium for that option is no higher than the premium for the pre-termination option.

Finally, any employee with an adjusted gross income of more than \$125,000 (or \$250,000, if married filing a joint return) is not eligible for the subsidy. Any premium subsidy received by such an individual will be recaptured through additional income taxes.

Subsidy Period

A terminated employee must pay 35% of the COBRA premium in order to qualify for the federal subsidy (and an employer must actually collect this 35% before requesting reimbursement of the other 65% from the federal government). This subsidy will be available to each eligible individual for up to nine months, beginning on the later of March 1, 2009, or the date the individual loses regular coverage under the plan. Thus, if an individual’s COBRA coverage commenced on October 1, 2008, this subsidy would be available for the nine-month period beginning on March 1, 2009.

Eligibility for this subsidy will end when a terminated employee is either offered other employer health coverage or becomes eligible for Medicare. Note that this standard differs from the standard under which COBRA coverage may be terminated. Termination of COBRA coverage is permissible only when an individual actually *obtains* coverage under another employer health plan, or becomes *entitled* to Medicare benefits. Thus, a terminated employee who becomes eligible for other employer coverage – but declines to enroll in that coverage – will lose the COBRA premium subsidy, but not the right to maintain his or her COBRA coverage.

Subsidy Mechanics

Although described as a federal subsidy, the initial payor of this 65% subsidy will be the employer sponsoring the plan under which the COBRA coverage is provided. (In the case of a *multiemployer* plan, the subsidy will be borne initially by the plan.) The employer will then recover the subsidy through a credit against the employer’s liability for employment taxes. These taxes may

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include federal income tax withholding, as well as both the employee and employer shares of FICA .

If this credit against employment taxes proves insufficient to recover the full premium subsidy, the employer will qualify for a direct payment from the federal government. This will be handled in the same way as an overpayment of employment taxes. Such a direct payment from the government will almost certainly be necessary for multiemployer plans because most do not have significant employment tax liabilities against which to claim the credit.

Recognizing that plan sponsors may not be able to implement this premium subsidy in time to meet the March 1 effective date, the bill contains a special provision for dealing with subsidy-eligible individuals who pay the full COBRA premium for either March or April coverage. The plan's sponsoring employer must either refund the 65% subsidy amount to the individual or credit the subsidy against the individual's future COBRA premiums.

Notice Obligations

Because this subsidy takes effect as of March 1, 2009, COBRA election notices should be promptly revised to refer to the subsidy's availability. (The statute does not appear to require any changes to the *general* COBRA notice.) The agencies responsible for COBRA enforcement are to draft model notices within 30 days after the Act becomes law (or by mid-March).

As noted above, any employees who were involuntarily terminated since September 1, 2008 – and who did not elect COBRA coverage when it was offered to them – must be given another opportunity to elect such coverage. A notice to that effect must be given to these individuals within 60 days of the Act's enactment (or by mid-April), along with any forms necessary for them to establish their eligibility for the premium subsidy.

They will then have 60 more days after receiving that notice in which to elect COBRA coverage.

Should such an individual actually elect COBRA coverage, that coverage need not be retroactive to the date of the loss of regular coverage. Rather, it need only take effect as of March 1, 2009. However, any resulting *gap* in coverage may not be counted toward a 63-day break in coverage that would otherwise cause the individual's creditable coverage to be lost, thereby subjecting the individual to another preexisting condition limitation or exclusion.

Maximum COBRA Coverage Period

Although this premium subsidy is limited to a period of nine months, nothing in the Act shortens the usual period of COBRA coverage. This remains 18 months following an employee's termination of employment.

Nor does anything in the Act *extend* the maximum COBRA period. As noted above, a provision in the House bill that would have entitled older or longer-service employees to maintain their COBRA coverage through age 65 was not included in the final Act. Although such a provision may yet resurface as part of a more comprehensive health care reform measure, employers should focus at this point on offering – and then recovering – the 65% premium subsidy.

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