

April 2009  
volume 7 number 1



## COBRA Premium Subsidies Under The American Recovery and Reinvestment Act

by James B. Yates and Sarah E. Pawlicki

On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act (ARRA), a.k.a.. the “Stimulus Bill,” into law. Employers just now are discovering some of the provisions contained within the law which will add to the responsibilities of the already overburdened Human Resources and Payroll Departments.

One such provision is the so-called COBRA subsidy contained within the ARRA.

### What Is The COBRA Subsidy?

COBRA is a federal law which provides individuals the opportunity to continue group health coverage under an employer’s group health plan in situations where the coverage would otherwise be terminated, i.e. separation from employment. Individuals electing COBRA coverage can be charged 102% of the applicable premium.

### Offices

#### Toledo Office:

One Seagate, 24th Floor  
P.O. Box 10032  
Toledo, Ohio 43699-0032  
Telephone: 419-241-6000  
Fax: 419-247-1777

#### Columbus Office:

100 E. Broad Street, Suite 600  
Columbus, Ohio 43215  
Telephone: 614-280-1770  
Fax: 614-280-1777


#### Findlay Office:

725 S. Main Street  
Findlay, Ohio 45840  
Telephone: 419-424-5847  
Fax: 419-424-9860

#### Novi Office:

28175 Haggerty Road  
Novi, Michigan 48377  
Telephone: 248-994-7757  
Fax: 248-994-7758

[www.eastmansmith.com](http://www.eastmansmith.com)



Under the ARRA, employees who were/are involuntarily terminated between September 1, 2008, and December 31, 2009, may be eligible to receive a 65% federal government subsidy for COBRA premiums for nine months.

### **Who Is Eligible To Receive The 65% Subsidy?**

The following requirements must be met for an individual to be considered an “assistance eligible individual” under the ARRA:

- An individual becomes a qualified beneficiary under COBRA between September 1, 2008 and December 31, 2009;
- The individual elects coverage; and
- The qualifying event triggering COBRA was an involuntary termination between September 1, 2008 and December 31, 2009.


### **Who Pays The Subsidy?**

Although the funds for the subsidy ultimately will be reimbursed by the federal government, the entity that currently pays the group health premiums will be responsible for initially paying 65% of the applicable premium and administrative fee. Assistance eligible individuals will be responsible for paying the remaining 35% of the applicable premiums and administrative fee.

As a practical matter, employers maintaining a group health plan and self-insured employers will be “fronting” the 65% subsidy and will later take a credit in the form of reduced payroll taxes. Multi-employer group health plans similarly will pay the 65% subsidy and subsequently take a tax credit.

### **How Does An Employer Get Reimbursed For The 65% Subsidy It Paid On Behalf Of Assistance Eligible Individuals?**

An employer paying the COBRA subsidy is reimbursed via a tax credit taken on quarterly payroll tax returns (Form 941 for 2009). The new form, recently published by the IRS, has two new lines (12a and 12b) for employer reporting of subsidies paid. The credit can be taken only if the individual actually pays the remaining 35% of the applicable premium. Numerous factors may complicate the reporting requirements — at least initially. First, most employers use software to complete payroll reports and those software programs will not have yet a field which contemplates the subsidy. Second, an employer’s payment of the subsidy could result in an overpayment of taxes which would be applied to the next tax return or requested as a refund. Third, an employer must decide if it wishes to reduce regular payroll deposits or wait until filing quarterly reports to claim the subsidy. Fourth, individuals who pay amounts greater than 35% (most likely to occur in March or April) either will have to be refunded the 65% subsidy or given a credit toward future premium payments. (The employer must choose between the two and



administer and account for the refunds/credits). Fifth, calculating the amount of the actual subsidy may be a challenge, particularly if the employer already pays a portion of the premiums for individuals electing COBRA. Finally, the IRS has cautioned that all employers claiming a subsidy credit should obtain and maintain supporting documentation such as:

- receipts for the 35% paid by the eligible individual;
- proof of invoiced amounts from, and proof of payment in full to, the insurance carrier;
- “attestation” of involuntary termination and date of involuntary termination;
- proof of the individual’s COBRA eligibility; and
- Social Security Numbers and amounts of subsidies reimbursed for each individual.

### **How Long Does The Subsidy Last?**

The 65% subsidy expires the earliest of the following:

- nine months after the “first day of the first month” that the individual receives the subsidy;
- the individual becomes eligible for another group health plan; or
- the maximum COBRA period expires.

Individuals must notify the group health plan if they become eligible for another group health plan.

### **When Can Individuals Begin Receiving (And When Must Employers Start Paying) Subsidies?**

Subsidized coverage begins with the “first period of coverage beginning on or after the date of enactment.” The date of enactment is February 17, 2009. For monthly period of coverage plans, subsidized coverage began March 1, 2009. There is a 60 day transition period to enable various parties to gear up for the new legislation. However, if individuals do not receive the COBRA subsidy on February 17, 2009 (or March 1, 2009 for monthly coverage plans), employers will be required to refund the subsidy or provide credit against future premiums.

### **How Are Individuals Notified About The Subsidy?**

Plan administrators must provide notices, which include information regarding the availability of the new subsidy, to all individuals who had/have qualifying events between September 1, 2008 and December 31, 2009 — regardless of whether the individuals already elected COBRA and regardless of whether the individuals are eligible for the subsidy. Those notices must be provided by April 18, 2009. Model notices are available from the Department of Labor.



## **What If Involuntarily Terminated Employees After September 1, 2008 Did Not Elect COBRA Coverage?**

Employees involuntarily terminated after September 1, 2008, are entitled to new COBRA notices containing information regarding the availability of the new subsidy and will be afforded 60 days to elect “second chance” coverage. COBRA eligibility under this scenario expires at the end of the original (not extended) period of continuation and the subsidy begins on February 17, 2009, (or March 1, 2009 for monthly period of coverage plans).

## **What If Involuntarily Terminated Employees Elected COBRA Coverage After September 1, 2008 But Stopped Paying Premiums?**

Employees who were involuntarily terminated after September 1, 2008 and elected COBRA but stopped paying premiums also are entitled to a new COBRA notice and 60 day election period. COBRA entitlement under this scenario also expires at the end of the original (not extended) period of continuation and the subsidy begins on February 17, 2009 (or March 1, 2009 for the monthly period of coverage plans).

## **If There Is A Coverage Gap For The Second Chance COBRA Electors, Do Pre-existing Condition Rules Apply?**

While COBRA coverage is not retroactive to the original date of COBRA eligibility, the pre-existing exclusions will not apply for the second chance electors — even if the break was 63 or more days.

## **Are Highly Compensated Individuals Eligible For The Subsidy?**

Highly compensated individuals are eligible for the subsidy, but the subsidy will result in increased tax liability at specific adjusted gross income thresholds. Tax liability is increased when an individual’s modified adjusted gross income reaches \$125,000 (\$250,000 if filing a joint return). If the individual’s income reaches \$145,000 (\$290,000 if filing a joint return), the full amount of the subsidy must be repaid as an additional tax. These individuals will be afforded an opportunity to disclaim the COBRA subsidy in the first instance and pay the unsubsidized amount.


## **Does The COBRA Subsidy Apply To All Types Of Coverage?**

The subsidy does not include COBRA premiums for flexible spending accounts (FSAs).

## **Can Employers Change Election Options?**

The ARRA provides that an employer may offer COBRA electors the option to select coverage different than the coverage the individual held on the date of the qualifying event. However, there are several conditions:



- 
- the premiums for these options must not exceed the premium for coverage formerly held by the individual;
  - the coverage options also must be available to active employees; and
  - individuals must be notified of these options and provided a 90 day election period. The different options must not provide merely vision, dental, counseling, on-site first aid or a flexible spending account.
  - between September 1, 2008, and December 31, 2009. Retirements, on the one hand

### **What About Individuals Terminated For Gross Misconduct?**

Individuals terminated for gross misconduct are not eligible for the COBRA subsidy.

### **Potential Areas Of Concern For Employers**

Employers must immediately determine who was “involuntarily terminated” versus. “voluntarily terminated” would generally be considered voluntary and, on the other hand, layoffs would generally be considered involuntary. However, many separations from employment will not fit squarely in either category. In these instances, employers should seek legal advice. Employers must work with third parties to identify all individuals (and obtain contact information for notices) with qualifying events between September 1, 2008, and December 31, 2009.

- To the extent the employer contracts with a third-party administrator for COBRA notice issues, will there be additional charges for the mandatory new notices?
- Employers who currently pay all or portions of COBRA premiums to terminated employees may wish to reconsider that policy.
- Employers will see an increase in group health insurance premiums as a result of anticipated increased COBRA elections. Individuals electing COBRA utilize health care coverage at a higher level than other individuals enrolled in the plan.
- Employers should coordinate with third-party administrators to send the new COBRA notices as soon as possible to shorten the election window.
- Employers must set up tracking mechanisms for COBRA eligibility and subsidy eligibility for employees involuntarily terminated including the second chance individual whose eligibility was no longer tracked due to non-election.
- Employers must set up systems to maintain additional documentation to support the Form 941 credit.

- Employers may have to deal with complaints from disgruntled highly compensated individuals who are forced to pay additional taxes as a result of electing COBRA and obtaining the subsidy. Forms must be developed to allow these individuals to decline the subsidy so as not to incur additional taxes.
- Employers will need to amend group health plan documents to incorporate the changes.

*Businesses with questions regarding the new COBRA subsidy coverage may contact Mr. Yates or Ms. Pawlicki at our Toledo office (419-241-6000).*



James B. Yates and Sarah E. Pawlicki are practicing lawyers in the Employment Group of the law firm of Eastman & Smith Ltd. Mr. Yates, a member of the Firm, represents public and private sector employers in all facets of labor and employment law.



Ms. Pawlicki, an associate, represents employers in employment discrimination and workers' compensation matters before administrative agencies as well as federal and Ohio courts.

#### **Disclaimer**

The articles in this newsletter have been prepared by Eastman & Smith Ltd. for informational purposes only and should not be considered legal advice. This information is not intended to create, and receipt of it does not constitute, an attorney/client relationship.