

COBRA Stimulus

Frequently asked questions

Q: What is the purpose of the new COBRA provisions in the American Recovery and Reinvestment Act of 2009 (aka the “stimulus” package)?

A: 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.

Q: How do the new provisions do this?

A: 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 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.

Q: What employers do the new COBRA provisions affect?

A: All employers that are subject to COBRA are subject to these provisions, as well as state and local employers covered under the continuation rules of the Public Service Health Act and plans sponsored by the federal government. In addition, the subsidy provisions apply to state continuation coverage that is comparable to federal COBRA. That would include so-called “mini-COBRA” state laws that cover groups below the 20 employee threshold for COBRA.

Q: When are the new provisions effective?

A: The new provisions apply to “premium[s] for a period of coverage beginning on or after the date of the enactment” of the bill, which was signed on February 17th, 2009. It appears that the new provisions will apply to any premiums for periods of coverage beginning on or after this date. Because most insurance contracts run on periods of coverage tied to calendar months, this means that in the vast majority of 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 mid-April.

Q: Who is eligible for the premium assistance?

A: Any “assistance eligible individual” or “AEI.” 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) originally lost coverage due to involuntary termination occurring during such period. Note that “AEIs” are not just involuntarily terminated employees. Because spouses and dependents are also “qualified beneficiaries” when an employee is terminated, they are also potential AEIs.

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

A: 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 COBRA 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.”

Example 1: Jane was involuntarily terminated from her job at XYZ Co., an employer subject to COBRA, on September 1, 2008. Jane was offered COBRA coverage but declined. Because Jane would have been an AEI had she had an election of COBRA continuation coverage in effect on February 17, 2009 (instead of never electing the coverage after her termination), she will get a second chance to elect COBRA.

Example 2: Walter was involuntarily terminated from her job at XYZ Co., an employer subject to COBRA, on September 1, 2008. Walter was offered COBRA coverage and elected it, but dropped the coverage after November 30, 2009 due to lack of payment. Because Walter would have been an AEI had he had an election of COBRA continuation coverage in effect on February 17, 2009 (instead of dropping the coverage on November 30), he will get a second chance to elect COBRA.

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Q: Do the new provisions change or replace other COBRA provisions?

A: 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.

Q: Are there any income limitations on the subsidy?

A: Yes. 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 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.

Q: Will the subsidized coverage extend the typical COBRA coverage time frame?

A: 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. It should be noted that the subsidy will likely cause AEIs to remain on COBRA for longer than normal qualified beneficiaries.

Q: Are there any other limitations on the subsidy, besides the nine month period?

A: Yes. 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 also not including 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.”

Q: 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?

A: 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%.

Q: How do potential AEIs who have already been terminated get notice of the subsidy?

A: This is the central question that plan administrators and third-party administrators are facing with this new law. Accordingly, the bill has directed the relevant federal agencies to have specific guidance (including “model notices” and the like) ready 30 days from the bill’s enactment.

Q: How is the subsidy going to be distributed?

A: 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.

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Q: Our company subsidizes COBRA coverage for some terminated employees. Can we recoup some of that money from the new required subsidy?

A: 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.

Q: How is the 2% COBRA administration fee accounted for in the subsidy?

A: The language of the bill does not expressly address this issue, so we will have to wait for further guidance. The general belief among industry observers, however, 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.

Q: What is the definition of “involuntary termination”?

A: The bill provides no definition of this phrase, which represents a significant departure from the usual COBRA practice of regarding terminations of any sort equally (notwithstanding gross misconduct). We anticipate forthcoming guidance to assist employers with this issue. Employers should consult with their legal advisors and determine for themselves who is an AEI. Please remember that the “involuntary termination” standard only has to do with the COBRA subsidy. Employees who voluntarily terminate (i.e., quit) must still be offered COBRA in the same manner they always have been.

Q: Will the federal government play any role other providing the subsidy and publishing guidance?

A: Yes, a very significant one. 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.

Q: Are there any other provisions to be aware of?

A: Yes. 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.



The Fessler Agency, Inc
3165 McMullen Booth Road, Bldg G2
Clearwater, Florida 33761
www.fessleragency.com
727-726-3377

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