

Stimulus Law Includes New Premium Subsidy for COBRA Beneficiaries

On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009, generally known as the economic stimulus law. The stimulus law creates new COBRA rules intended to help those who lose group medical plan coverage due to an involuntary termination of employment between September 1, 2008 and December 31, 2009. These individuals, referred to as “assistance eligible individuals,” will be entitled to a nine-month, 65 percent federal subsidy of the required COBRA premiums. The new COBRA rules also require employers to develop new COBRA notice documentation and COBRA payment administration procedures.

The New COBRA Premium Subsidy

Under the stimulus law, the federal government will pay – for up to nine months – a subsidy equal to 65 percent of the COBRA premium charged to an assistance eligible individual; the individual will be required to pay the remaining 35 percent. However, if an employer provides a period of coverage without charge (or at a reduced rate) as part of a severance program, then there will be no subsidy (or a subsidy based on the reduced rate).

The subsidy applies to periods of COBRA continuation coverage beginning after the February 17 enactment of the stimulus law. A period of coverage is the monthly (or shorter) period for which COBRA premiums are charged. If premiums are charged on a calendar month basis, then the subsidy will be applied starting March 1, 2009. The subsidy ends when the earliest of these milestones occurs:

- An individual becomes eligible for subsequent coverage;
- The nine months following the first subsidy expires; or
- The maximum COBRA coverage period expires.

Employers also are required to provide cash refunds or credits to assistance eligible individuals who pay the full COBRA premium for coverage while the subsidy applies.

New Special COBRA Election Period

The new law also requires that certain individuals who did not have COBRA benefits must be given a second chance for coverage. This would include, for example, anyone who would be assistance eligible except that he or she did not elect COBRA coverage when previously eligible, or an individual who is no longer covered by the group health plan due to not having paid the COBRA premium.

The new, special election period begins February 17 and ends 60 days after the plan administrator provides the newly required COBRA notice to assistance eligible individuals. Employers must act immediately to identify these individuals and develop administrative procedures to provide a new COBRA notice in compliance with the new rules. The stimulus law requires the U.S. Department of Labor to issue a model notice to satisfy these requirements by March 19, 2009.

Employer's Paid COBRA Premium Subsidy Through Payroll Tax Credit

The federal government will “pay” the subsidy by allowing employers to claim a credit equal to the subsidy against the requirement to make deposits or payments of payroll taxes, such as income tax withholding, employee FICA withholding, and employer FICA taxes. An employer is not allowed to take the payroll tax credit until the assistance eligible individual pays the subsidized premium. The federal government will make a direct payment to the employer for any portion of the subsidy that cannot be recovered by means of a credit.

There are rules that require an employer to account for each individual for whom the subsidy is provided and to report detailed information about the subsidy to the IRS. There is no guidance, however, about how to submit the information under the current payroll tax deposit rules or the rules for quarterly payroll tax reporting. We expect the IRS to issue guidance and revise the applicable tax forms in the near term.

Other Issues

The new rules contain other provisions. For example:

- Employers are permitted (but not required) to allow assistance eligible individuals to change levels or types of coverage if certain conditions are met.
- The provisions specify that the subsidy is not taxable income to the assistance eligible individual.
- There is a “recapture tax” imposed against high-annual-income individuals (\$145,000 single, \$290,000 married) who receive the subsidy; this has the practical effect of excluding this group from the subsidy; the plan administrator must allow these individuals the option to waive the subsidy to avoid the “recapture tax.”

What Employers Should Do Now to Comply

Employers should begin immediately to learn about the new COBRA rules under the stimulus law. Employers also should watch for more guidance about the new rules in the coming days. Until such guidance is available, employers should:

- Identify all assistance eligible employees (past and future);
- Develop plans to notify assistance eligible employees of the new COBRA rules;
- Determine the correct premium subsidies to apply;
- Develop accounting and other processes to capture data needed to seek the federal subsidy and report the detail when required;
- Amend plan documents, plan group insurance contracts, and plan administration contracts; and/or
- Contact the plan's COBRA administrator and ensure compliance steps are taken.

Conclusion

Accurate and reliable COBRA compliance is always an important tool for employers to control and limit liabilities under group medical plans. A single mistake in COBRA compliance can result in significant claim liability that could have been avoided with complete and accurate COBRA administration. The advent of the new COBRA subsidy and related issues will only heighten the need for COBRA compliance. Employers must pay attention to these new rules and act now to ensure compliance.

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