Additional Guidance Released on COBRA Premium Assistance

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NEWS ALERT

We previously published an article describing the premium assistance and other relief provided under the American Recovery and Reinvestment Act of 2009 (the "Act"), which was enacted on February 17, 2009. Even though the provisions of the Act were effective immediately, no guidance was issued at that time and many employers and plan administrators were left wondering what the new law meant to them. To address the initial lack of guidance, the Internal Revenue Service (the "Service") and the Department of Labor (the "DOL") have been feverishly publishing information and holding joint webcasts with the Department of Treasury. Last week, the Service issued Notice 2009-27, which provides significant insight into many of the questions that were left unanswered by the Act. In addition, the DOL updated its website to clarify the plan administrator's notice obligations under the Act. This article provides a summary of the key topics that are covered under this new guidance.

Background

The Act provides premium assistance for "assistance eligible individuals." For these purposes, an "assistance eligible individual" (an "AEI") is defined as any qualified beneficiary who, between September 1, 2008 and December 31, 2009, is eligible for COBRA continuation coverage as a result of a covered employee's involuntary termination of employment during that period and who actually elects the coverage. The term "COBRA", for purposes of the Act, includes continuation coverage provided under the Consolidated Omnibus Budget Reconciliation Act of 1985, the Public Health Service Act, and similar laws.

Involuntary termination

Although a covered employee is required to suffer an involuntary termination in order to receive premium assistance, the Act did not provide a definition of "involuntary termination" for this purpose. In Notice 2009-27, the Service now defines "involuntary termination" as "a severance from employment due to the independent exercise of the unilateral authority of the employer to terminate the employment, other than due to the employee's implicit or explicit request, where the employee was willing and able to continue performing services." Although the definition appears to be relatively straightforward it does not indicate the breadth of situations that are intended to be encompassed under the Act. The notice includes numerous examples of fact-specific situations that the Service has concluded would be considered an involuntary termination for purposes of the Act, including:

- An employee's voluntary participation in an employer's severance program;
- A voluntary termination for good reason due to the employer's action that causes a material negative change in the employment relationship for the employee;
- An involuntary termination for cause (but not for gross misconduct);
- An involuntary reduction to zero hours (such as pursuant to a layoff, furlough or other suspension of employment), which results in a loss of health coverage;
- An employee's voluntary termination following an involuntary reduction in hours;
- An employer's action to terminate the employee's employment as a result of the employee's absenteeism due to illness or disability;
- An employee's voluntary retirement if the employer would have terminated the employee's services and the employee had knowledge that the employee would be terminated;
- The employer's failure to renew a contract at the time the contract expires if the employee was willing and able to execute a new contract providing terms and conditions similar to those in the expiring contract and to continue providing services;
- and An employer-initiated lockout (but not a work stoppage from a strike initiated by employees or a union).

Of importance, the Service specifically concluded that death is not an involuntary termination under the Act. Consequently, a covered employee's spouse and dependent children are not eligible for premium assistance as a result of the employee's death during the applicable period.

Coverage eligible for premium assistance

According to the Act, an AEI is eligible for premium assistance for continuation coverage under any health plan, other than a flexible spending arrangement that is provided under a cafeteria plan. In response to numerous questions, the Service reiterated in Notice 2009-27 that premium assistance applies to dental-only and vision-only plans, even if the benefit is paid entirely by employees. In addition, the Service clarified that premium assistance applies to health reimbursement arrangements (since these arrangements are not offered under cafeteria plans) and to retiree health coverage that constitutes COBRA continuation coverage (i.e. it does not differ from the coverage provided to similarly situated active employees, other than with respect to the higher premium charged).

Application for premium assistance

Pursuant to the Act, an AEI is entitled to continuation coverage for any period in which coverage is elected on or after February 17, 2009 if he pays 35% of the applicable COBRA premium otherwise required for such coverage. The Service has previously stated that an employer may not automatically reduce the premium for an AEI; rather, an individual who believes that he is an AEI entitled to premium assistance under the Act is required to apply to the group health plan to be treated as such. For this purpose, the DOL has published a model application to be distributed with the revised election forms. It remains unclear, however, whether an individual who is a "high income individual" (i.e. generally, an individual with modified adjusted gross income over $125,000 or, in the case of married taxpayers filing jointly, $250,000), and whose taxable income would otherwise be increased by all or a portion of the premium assistance provided under the Act, is required to affirmatively waive the premium assistance, as stated in the Act, or may simply decline to apply for it. Neither the Service nor the DOL have addressed this point.

Calculation of premium assistance

The Service explained in Notice 2009-27 that the reduced premium is calculated based on the cost that must be paid by or on behalf of the AEI for continuation coverage under the group health plan. Consequently, if a group health plan charges $1,000 for continuation coverage, and such cost includes the 2% administrative fee for such coverage, the AEI would be required to pay $350 (or 35% of $1,000) for continuation coverage during the premium assistance period provided under the Act and the employer would be entitled to a payroll tax credit in the same amount for such period. If, however, the AEI's share of the cost is only $500, then, during the premium assistance period provided under the Act, the AEI would be required to pay $175 (or 35% of $500) for continuation coverage and the employer would be entitled to a payroll tax credit in the same amount. Where the cost of continuation coverage is paid entirely by the employer, no premium assistance (and, hence, no payroll tax credit) would apply.

Coverage for non-assistance eligible individuals

The Service also explains in Notice 2009-27 how to calculate the premium assistance for continuation coverage that is being provided to one or more individuals who are not qualified beneficiaries under the Act, such as domestic partners. To determine the applicable cost to which the premium assistance applies, the amounts paid for coverage are allocated first to the cost of covering AEIs and then to the cost of covering non-AEIs. Consequently, if the cost of covering the non-AEIs does not add to the cost of covering the AEIs, then the cost of covering the non-AEIs is zero, and the premium assistance will apply to the full amount paid for continuation coverage under the group health plan. If, however, the cost of covering a non-AEI adds to the cost of covering the AEIs, then the incremental cost is ineligible for premium assistance under the Act.

Subsidy applies to increased premium

Interestingly, in Notice 2009-27, the Service states that employers who have previously charged less than the maximum COBRA premium may increase the premium charged under the group health plan in order to receive the payroll tax credit available under the Act. If a lower premium payment is currently provided under an employment or severance agreement with the covered employee, the employer may agree to provide for a separate taxable payment to be made to the AEI as consideration for the increase in the COBRA premium.

Length of premium assistance period

The Act provides that premium assistance applies to the first period of coverage beginning on or after February 17, 2009 and generally extends for the nine (9) month period beginning on the first day of the month on which the premium assistance applies. For plans that permit partial coverage periods calculated from the date on which the loss of coverage occurs, it is unclear whether the 9-month period begins with the partial month of coverage or with the first calendar month for which coverage is provided thereafter. During the second joint webcast sponsored by the Service, DOL and Department of Treasury on April 6, 2009, a representative of the Department of Treasury indicated that it had not yet resolved this issue but expected additional guidance to be released within the coming months.

In addition, the Service explains that the application of the premium assistance period will depend on how the employer treats the provision of continued coverage following the covered employee's involuntary termination. For example, if an employer allows a covered employee and his qualified beneficiaries to participate in the group health plan on the same basis as active employees for the 6-month period following the covered employee's involuntary termination, and the employer treats the loss of coverage as occurring at the end of such 6-month period, then the covered employee and his qualified beneficiaries will be eligible to elect continuation coverage at the end of the 6-month period and, likewise, will be eligible to receive premium assistance for the first 9 months of such continuation coverage. Alternatively, if the employer treated the loss of coverage as occurring coincident with the involuntary termination of employment, the 9-month period for which the covered employee and his qualified beneficiaries would be eligible for premium assistance under the Act would commence coincident with the 6-month period of coverage provided by the employer (or the first day of the first calendar month in such 6-month period that begins after February 17, 2009, if later).

As a general matter, the period for premium assistance under the Act is terminated upon the earlier of the date the AEI becomes eligible for other major medical coverage or Medicare or the date on which the maximum COBRA continuation coverage period expires. In Notice 2009-27, the Service explains that an individual's eligibility for retiree coverage that is not COBRA continuation coverage will not be treated as eligibility for other major medical coverage for these purposes if either (a) the retiree coverage is offered under the same plan as the COBRA continuation coverage or (b) the retiree coverage is offered under a different plan from the COBRA continuation coverage, the individual's eligibility for such coverage arose between September 1, 2008 and February 16, 2009, and the individual's right to enroll in such coverage ended before February 17, 2009. Under all other circumstances, the individual's eligibility for retiree coverage will result in early termination of premium assistance under the Act.

Notices and required actions

The DOL clarified that, notwithstanding the language in the Act, not all qualified beneficiaries are required to receive a revised COBRA notice with information about premium assistance. According to the updated Q&As on the DOL's website, a new COBRA notice is not required with respect to an individual who had a qualifying event other than an involuntary termination during the applicable period and received an otherwise compliant election notice under COBRA (without regard to the changes made by the Act) before February 17, 2009. This is welcome news for plan administrators!