



## Management Alert

# COBRA Subsidy in Stimulus Package to Benefit Involuntarily Terminated Employees

The COBRA provisions of the American Recovery and Reinvestment Act of 2009 (the "Act") provide for an employer subsidy of COBRA premiums for involuntarily terminated employees. The new law will have a substantial impact on employers' ongoing obligations under COBRA. This Management Alert summarizes the COBRA provisions of the economic stimulus bill and discusses how employers may be impacted by the new law.

### How the Subsidy Works

An "assistance eligible individual" will only be required to pay 35% of his or her COBRA premium. The remaining 65% of the COBRA premium will be reimbursed by means of a payroll tax credit to the employer (in the case of a self-funded plan), the plan (in the case of a multiemployer plan), or the insurer (in the case of an insured plan that is not subject to federal COBRA). The Secretary of the Treasury will issue guidance on how a claim for the tax credit is to be filed. If the payroll tax credits are insufficient to cover the COBRA expense, then the entity entitled to reimbursement will receive the remainder of reimbursement directly from the Secretary of the Treasury.

### Who is Eligible

An assistance eligible individual ("Eligible Individual") is a person who becomes eligible for COBRA between September 1, 2008 and December 31, 2009 due to a covered employee's involuntary termination of employment. The subsidy applies to spouses and dependents who are eligible for COBRA coverage as well.

If an individual is denied treatment as an Eligible Individual by a group health plan, the Act requires the Department of Labor to provide for an expedited review of such denial.

### Income Limitations

The full subsidy is only available for individuals with a modified adjusted gross income of up to \$125,000 (\$250,000 for joint filers) or less for the taxable year in which the subsidy is received. A reduced subsidy is available if the individual's modified adjusted gross income is between \$125,000 and \$145,000 (\$250,000 and \$290,000 for joint filers). If a subsidy is provided with respect to an individual whose modified adjusted gross income exceeds these limitations, the Act provides by its terms that the individual's income tax liability is increased by the amount of the subsidy. As the recapture appears to be structured as a dollar for dollar increase in tax liability, an individual who is concerned that he may exceed these limitations may want to waive the subsidy. However, the subsidy may not be recovered if the individual later determines that the income threshold was not exceeded.

## Duration of Subsidy

The subsidy will be available for nine months, but not beyond the end of the maximum period of coverage required under COBRA or the individual's becoming entitled to coverage under another group health plan or Medicare.

## Special Election Period

Individuals who would have qualified as an Eligible Individual except that they had not elected COBRA as of February 17, 2009 have a special 60-day election period under the Act. The election period begins February 17, 2009 and ends 60 days after the date notice of the subsidy is provided. If an employee elects COBRA during this special election period, coverage shall commence with the first period of coverage beginning after February 17, 2009 and will not go beyond the period of COBRA coverage that would have been required if COBRA had been initially elected.

## Lower-Cost Health Plan Options

Generally under COBRA, qualified beneficiaries can only elect to continue the coverage that they had immediately before the qualifying event. However, an employer may permit qualified beneficiaries who are eligible for the COBRA subsidy to elect a lower-cost health plan option available under the employer's plan. This option will be available only if the coverage is not (a) coverage that provides only dental, vision, counseling, or referral services, (b) a flexible spending arrangement, or (c) coverage for services or treatments furnished in an on-site medical facility maintained by the employer and that consists primarily of first-aid services, prevention and wellness care, or similar care.

## Notice Requirements

The Act requires that the existing COBRA notice be modified to contain additional information about the availability of the subsidy, the availability of any lower cost health plan options, the obligation of a qualified beneficiary to notify the plan of eligibility under another plan, and the penalty for failure to provide this notice. In addition, notice must be given to qualified beneficiaries entitled to the special election period described above. The Secretary of Labor is required to prescribe model notices within 30 days of enactment of the Act.

## Effective Date

The subsidy will apply to premiums paid for periods of COBRA coverage beginning on or after February 17, 2009.

## Employer Considerations and Impact of the Law

- Employers should review their severance arrangements and health plan documents to determine how these plans and programs will be affected by the new law.
- It is not clear whether the subsidy will be available if the employer provides free post-termination coverage or the employee pays less than 35% of the COBRA premium (as may be the case if the former employee pays active employee rates) because a literal reading of the Act requires the Eligible Individual to pay 35% of the premium. Therefore, employers should consider whether it is more beneficial to pay for continued coverage as part of a severance arrangement or to only offer employee-pay-all COBRA.

- Employers or plan administrators should update their COBRA forms and notices and/or contact their third party administrator to ensure compliance with the new law.
- Employers or plan administrators should inform their payroll personnel and vendors as to the premium reimbursements that will be treated as payroll tax credits and make the appropriate application.
- Employers should also take steps to determine which involuntarily terminated employees are Eligible Individuals, as notice of the special election period described above must be provided within 60 days after the enactment of the Act.

*For additional information, please contact the Seyfarth attorney with whom you work, or any Employee Benefits attorney on our website at [www.seyfarth.com/EmployeeBenefits](http://www.seyfarth.com/EmployeeBenefits).*



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