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Federal Stimulus – Group Coverage Continuation Subsidy

Version As of: March 17, 2009

On February 17, 2009, President Barack Obama signed the American Recovery and Reinvestment Act, commonly called the Stimulus Plan. The new law provides a subsidy to employees and their dependents that may reduce the cost of COBRA and other comparable group state continuation coverage by 65 percent for qualified beneficiaries who become eligible due to the covered employee's involuntary termination of employment between September 1, 2008 and December 31, 2009. These individuals are referred to as Assistance Eligible Individuals (AEIs.)

Unless otherwise specified, for purposes of the American Recovery and Reinvestment Act and this summary, the term "COBRA" means continuation coverage provided under:

- ERISA
- The Public Health Services Act
- Section 4980B of the Internal Revenue Code
- Any State law that provides continuation coverage comparable to COBRA. Pending further federal guidance, Trustmark is analyzing what constitutes comparable continuation coverage.

The definition of qualified beneficiary includes:

- the covered employee
- the covered employee's spouse (as defined by federal law), and
- the covered employee's dependent children (as defined by the plan)

What are the key changes the American Recovery and Reinvestment Act introduces to COBRA?

- A 65 percent subsidy of COBRA premiums, for up to nine-months, to assist employees and dependents impacted by the employee's involuntary termination of employment.
- The employer, multi-employer plan (defined in ERISA as a plan maintained under a collective bargaining agreement to which more than one employer is required contribute), or the insurer in some instances involving state continuation is responsible to pay the 65 percent subsidy, which is reimbursed in the form of a payroll tax credit
- The creation of an additional 60-day election period to allow AEIs who previously declined federal COBRA or who enrolled for federal COBRA but later lost such coverage to re-elect federal COBRA coverage with subsidized premiums. This special election period does not apply to state continuation unless the state enacts legislation requiring otherwise.
- Additional notice requirements

Who is entitled to the subsidy?

AEIs are eligible for the subsidy. They consist of employees who are COBRA qualified beneficiaries and meet specific criteria.

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1. The individual must experience a qualifying event that is an involuntary termination of employment (except in the case of gross misconduct),

2. The qualifying event must take place between September 1, 2008 and December 31, 2009, and

3. The individual must elect COBRA during their initial election period or the additional, 60-day election period. The additional 60-day election period does not apply to state continuation unless the state enacts legislation requiring otherwise.

When will eligible individuals first receive the subsidy?

The subsidy applies beginning with the first period of coverage after the date of enactment. For example, if the plan requires individuals to pay premiums on a monthly basis, the first period begins March 1, 2009.

How much will AEIs pay for premiums?

AEIs are required to pay 35 percent of the premium that he or she would have otherwise been required to pay.

Example 1:

- 102 percent of the cost of coverage under the group health is $1,000
- Employer charges $1,000 to purchase COBRA
- The AEI is required to pay 35 percent of $1,000 or $350
- The employer would pay the remaining 65 percent, or $650 and then offset via a payroll tax credit

Example 2:

- The active employee premium is $500
- Due to a severance agreement the former employer subsidizes 50 percent of the premium and the former employee pays $250
- Under the new law the former employee is an AEI and therefore eligible for the subsidy
- The AEI is then responsible for 35 percent of the $250 premium ($87.50) and the former employer receives 65 percent of the other $250 ($162.50) via payroll tax credit

Is there an income limitation for the subsidy?

Yes. All AEIs are eligible for the subsidy but depending on their income, certain individuals could be required to repay the subsidy as an additional income tax called a “recapture tax”. The income rules apply on a taxable year basis so a taxpayer might be required to repay the subsidy in one taxable year and not another if the subsidy period crosses over from one calendar year to the next.

AEIs with modified adjusted gross income of less than $125,000 (individual) or $250,000 (joint) are not subject to the recapture tax.

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For AEIs with modified adjusted gross income between $125,000 and $145,000 (individual) and $250,000 and $290,000 (joint) the subsidy is phased out using a ratio described in the law.

AEIs with an adjusted gross income exceeding $145,000 (individual) and $290,000 (joint) would be required to repay the subsidy in full.

What coverage does the subsidy apply to?

The subsidy applies to all health plans subject to federal COBRA with the exception health of Flexible Spending Accounts (FSAs.) In addition, the subsidy applies to small employer group coverage (< 20 employees) that is not subject to federal COBRA rules, but instead subject to "comparable" state continuation laws.

Does an employer have to offer additional COBRA coverage options?

Employers are not required to offer AEIs options to enroll in group health plan options other than the option that the AEI was enrolled in at the time of the qualifying event.

If an employer chooses to allow additional options, the new coverage option must have the same or lower premium as the individual's previous coverage.

How long does the subsidy apply?

The subsidy will apply for the first period of coverage beginning after the date of enactment of the law. For example, if premiums are charged on a monthly basis, the subsidy will begin on or after March 1, 2009 and will last for up to nine months.

Are there situations in which AEIs would not receive the full nine months of subsidized premiums?

Yes, the subsidy can end earlier for any of the following reasons:

- The AEI becomes <u>eligible</u> under another group health plan or Medicare
- The AEI reaches the end of the maximum period of coverage before the nine months elapses, or
- The AEI elects COBRA during the 60-day election period and reaches the end of the maximum COBRA coverage period (extending from the AEIs initial COBRA election period) before the nine months elapses

Any AEI who becomes eligible for other group health coverage or Medicare must provide notice that he or she no longer qualifies for the subsidy. *Failure to do so is punishable by a penalty equal to 110 percent of the subsidy received after becoming eligible for other coverage*.

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Will eligible individuals who previously terminated or declined to elect group continuation coverage have another opportunity to elect COBRA coverage and receive the subsidy?

Yes. If you were eligible for federal COBRA coverage by reason of an involuntary termination of employment on or after September 1, 2008 and you initially declined to elect federal COBRA coverage, or elected COBRA coverage and later stopped paying premiums, you will receive notification of an additional opportunity to elect COBRA and receive the subsidy.

Coverage for those individuals who experience an involuntary termination of employment prior to March 1, 2009 and who elect COBRA during the additional election period will become effective for coverage on March 1, 2009. Coverage will not be reinstated retroactively to the original loss of coverage date. This additional election right does not apply to state continuation coverage unless the state enacts legislation requiring otherwise.

In addition, any gap in coverage between the date coverage is lost and the enactment date will not be considered a break in coverage for purposes of HIPAA's pre-existing condition exclusion rules.

What are the additional notice requirements mandated under the American Recovery and Reinvestment Act?

The Department of Labor is expected to provide model language for use by employers and insurers within 30 days of the date of enactment of the law.

Notices are required to be sent 60-days from the date of enactment.

A notice is required to be sent to those individuals who are subsidy-eligible and have already elected COBRA coverage. The notice must advise them of the subsidy and how it works.

Another notice is required to all individuals who had a COBRA qualifying event between September 1, 2008 and December 31, 2009, not just to those individuals who were involuntarily terminated during that time period. This notice will inform individuals of the opportunity to elect continuation coverage with subsidized premiums.

IMPORTANT: Employers should identify AEIs as soon as possible so necessary notification and payroll actions can be taken.

What entity receives the tax credit?

Generally, it is the employer that provides the subsidy and is eligible for the payroll tax credit, subject to two exceptions. First if the plan is a multi-employer plan, then it is the plan that is eligible for the payroll tax credit. Second, if fully insured COBRA coverage is provided under state continuation coverage, then the insurer is the one eligible for the payroll tax credit if the insurer paid the 65 percent subsidy.

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How does the payroll tax credit work?

The employer, multi-employer plan, or insurer recoups the subsidy by claiming a credit equal to the subsidy against the requirement to make deposits or payments of payroll taxes. Payroll taxes are defined as income tax withholding, employee FICA withholding, and employer FICA taxes.

The IRS has recently issued guidance regarding the Payroll Tax Form (Form 941) that must be used to claim this credit available at:
http://www.irs.gov/newsroom/article/0,,id=204709,00.html

Additional guidance for employees is available from the U.S. Department of Labor at:
http://www.dol.gov/ebsa/faqs/faq-consumer-cobra2.html

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