

Employee Relations

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Employee Benefits

Recent Legislative Changes Require Immediate Employer Action and Point to Future Trends

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This column discusses the changes to COBRA rules contained in the recent economic stimulus bill—the American Recovery and Reinvestment Act of 2009—as well as the new federal Children’s Health Insurance Program Reauthorization Act, which funds the State Children’s Health Insurance Program (SCHIP), and changes in the Mental Health Parity Act. The so-called COBRA changes made to the law in 1985 have had a significant effect on employer health plans, and the law “must be doing something right” in the eyes of Congress as that body cannot resist tinkering and expanding the law further. The recent economic stimulus bill continues this trend, with a provision effective immediately that contains portentous change. For the first time, the government has undertaken to subsidize *directly* part of the COBRA costs for “assistance eligible individuals.” (Of course, the existing tax benefits for such coverage are a significant indirect subsidy.) As explained below, this change and the additional changes discussed in this article point to more mandated “partnerships” by employers with the government in the realm of health care.

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COBRA Changes

Background

COBRA is the acronym for the well-known law that requires group health plans to offer certain individuals (“qualified beneficiaries”) the opportunity to continue their group health plan coverage for a specified period of time (“continuation coverage”) after certain events that otherwise would have terminated their participation (“qualifying events”). This coverage must be identical to the coverage provided under the plan to similarly situated non-COBRA beneficiaries with respect to whom a qualifying event has not occurred. The qualified beneficiary may be charged for the coverage. The amount of such premium generally may not exceed 102 percent of the “applicable premium” for such period and the qualified beneficiary must have the opportunity to pay the premium in monthly installments.

The maximum required period of continuation coverage for a qualified beneficiary depends on the specific qualifying event that gives rise to a qualified beneficiary’s right to elect continuation coverage. In the case of a termination of employment or reduction of hours that results in the right to elect coverage, the minimum period of coverage that must be offered begins with the loss of coverage on account of the qualifying event and ends on the date that is 18 months after the date of the qualifying event. Such coverage could also end earlier if: (1) the employer ceases to provide any group health plan to any employee; (2) the covered beneficiary fails to pay premiums; or (3) the qualified beneficiary becomes (after the date of election of continuation coverage) covered under any other group health plan or Medicare. The minimum election period under which a qualified beneficiary is entitled to elect continuation coverage begins not later than the date on which coverage under the plan terminates on account of the qualifying event, and ends no earlier than the later of 60 days or 60 days after notice is given to the qualified beneficiary of his or her COBRA rights.

Rationale for the Changes

The ability to continue employer-provided coverage after termination of employment under COBRA is welcome relief to persons who lose health care coverage upon voluntary or involuntary termination of employment. But many workers, accustomed to employer-subsidized health benefits, are shocked at the cost of the COBRA premiums, which on average can exceed \$4,000 for single coverage and \$10,000 for family coverage. Workers who are unwilling or unable to afford these costs often become uninsured.

As part of the American Recovery and Reinvestment Act of 2009 (the Act), Congress decided to *subsidize*, on a limited basis, up to 65 percent

of the cost of COBRA premiums for eligible workers who are “involuntarily terminated,” other than for cause, in order to assist temporarily workers who lose their coverage. As discussed herein, the subsidy is paid to the employer or other entity that provides the coverage, and will be paid as a credit against payroll taxes after the employer incurs the initial cost.

Expanded Coverage Under the Stimulus Act

It is important to note that the Act expands the subsidy beyond the plans subject to the federal COBRA rules. Continuation coverage that qualifies for the subsidy also includes continuation coverage required under state law that requires continuation coverage comparable to the continuation coverage required under the IRC’s COBRA rules for group health plans. This means that certain *small* (fewer than 20 employee) health plans otherwise exempt from COBRA or health plans maintained by the federal government or a state government may be eligible for the subsidy, and those plans and their insurers will have to administer the new rules, including the notices and reimbursement provisions.

Immediate Effective Date

The Act was effective almost immediately. Signed on February 17, 2009, it creates a subsidy (effective for the first payment period after enactment) for persons involuntarily terminated from employment between September 1, 2008, and December 31, 2009. Notification of eligibility must begin within 60 days of the Act, although as discussed below, the subsidy is available for periods after the statute’s enactment.

General Rules

The new law provides a 65 percent subsidy for COBRA premiums paid by an “assistance eligible individual” for a period of up to nine months. That means such individuals must receive COBRA coverage if they pay 35 percent of the premium cost. The law operates by treating such individuals as having paid any premium required for COBRA continuation coverage under a group health plan if the individual pays 35 percent of the premium. This required amount can be higher after certain income levels.

New COBRA Notices

The individual has a special 60-day period to elect such coverage beginning on the date notice is provided. In addition to the information

required for COBRA notices, the notice of COBRA continuation coverage to a person eligible for a subsidy must contain additional information including information about the qualified beneficiary's right to the premium reduction (and subsidy), the conditions for the subsidy, and a description of the obligation of the qualified beneficiary to notify the group health plan of eligibility under another group health plan or eligibility for Medicare benefits, and the penalty for failure to provide this notification. Model Notices have been made available by the Department of Labor. Information about these notices, and answers to other frequently asked questions, can be found at www.DOL.gov/COBRA.

Eligible Individuals

An individual is eligible for the subsidy if he or she meets the following requirements. First, the qualifying event with respect to the covered employee must be a loss of group health plan coverage due to an *involuntary termination* (other than for gross misconduct). The subsidy would also apply to coverage for other individuals who are covered under the involuntarily terminated employee's plan and who are qualified beneficiaries as a result of the termination. Note that by contrast, the eligibility criteria for regular, unsubsidized COBRA—which has not changed—is for *any* termination of employment, voluntary or involuntary, other than for gross misconduct.

To qualify for the subsidy, the qualifying event (the involuntary termination) must occur during the period beginning September 1, 2008, and ending December 31, 2009, and the qualified beneficiary must be eligible for COBRA continuation coverage during that period and elect such coverage.

The qualified beneficiary cannot have modified adjusted gross income that exceeds \$145,000 (or \$290,000 for joint filers) in the taxable year that they are receiving the subsidy. Any premium paid in excess of the amount allowed in a year must be repaid. It appears that it is intended that the qualified beneficiary is responsible for monitoring the income requirement. The mechanism for repayment is an increase in the taxpayer's income tax liability for the year equal to such amount. For taxpayers with adjusted gross income between \$125,000 and \$145,000 (or \$250,000 and \$290,000 for joint filers), the amount of the premium subsidy for the taxable year that must be repaid is reduced "proportionately." An individual could be ineligible one year and eligible in the next. The legislative history explains the repayment mechanism as follows:

For example, an assistance eligible individual who is eligible for Federal COBRA continuation coverage based on the involuntary termination of a covered employee in August 2009 but who is

not entitled to the premium subsidy for the periods of coverage during 2009 due to having income above the threshold, may nevertheless be entitled to the premium subsidy for any periods of coverage in the remaining period (e.g., 5 months of coverage) during 2010 to which the subsidy applies if the modified adjusted gross income for 2010 of the relevant taxpayer is not above the income threshold.

Length and Effect of Subsidy

The subsidy is paid until the first month beginning on or after the earlier of: (1) the date which is nine months after the first day of the first month for which the subsidy applies; (2) the end of the maximum required period of continuation coverage for the qualified beneficiary under the COBRA rules or the relevant state or federal law (or regulation); or (3) the date that the assistance eligible individual becomes *eligible for* another group health plan or Medicare. The basis for ending the subsidy is *eligibility*, not actual coverage. Eligibility for coverage under another group health plan does not terminate eligibility for the subsidy if the other group health plan provides only dental, vision, counseling, or referral services (or a combination of the foregoing), or is a health flexible spending account (FSA), or health reimbursement arrangement.

The qualified beneficiary must notify the group health plan of such eligibility under the other plan or Medicare; failure to do so can result in a penalty equal to 110 percent of the subsidy provided after termination of eligibility. The notification must be provided to the group health plan in the time and manner as is specified by the Secretary of Labor.

Any subsidy provided is excludible from the gross income of the covered employee, and not counted as income for purposes of other income-related government programs. For purposes of determining the gross income of the employer and any welfare benefit plan of which the group health plan is a part, the amount of the premium reduction is intended to be treated as an employee contribution to the group health plan.

Option to Change Coverage

In addition, although under COBRA a qualified beneficiary is generally only entitled to the type of coverage he or she had elected before the qualifying event, the law permits a group health plan to provide a special enrollment right to assistance eligible individuals to allow them to *change* coverage options to elect a *less* expensive option under the plan in conjunction with electing COBRA continuation coverage. This differs from the current COBRA rules and is designed to reduce the employee's (and government's) costs. This does not change the basic COBRA continuation coverage requirement that a group health plan allow an eligible

individual to choose to continue with the coverage in which the individual is enrolled as of the qualifying event. However, once the election of the other coverage is made, it becomes COBRA continuation coverage under the applicable COBRA continuation provisions.

Effective Date

The COBRA provision is effective *immediately* upon enactment. For most employers the subsidy is effective starting March 1, 2009. This means that employers must modify their COBRA notices as soon as possible to explain the subsidy. Otherwise, an affected individual could argue that he or she would have elected COBRA coverage had he or she known the cost would be less. The law does not address that issue, but recognizing that plans may need time to implement the new law, the law allows plans to charge 100 percent of the premium for 60 days after enactment and “make up” the subsidy with either a reduction in future premiums or a flat payment (if the reduction is not workable because, for example, the coverage period has ended).

The provision applies to all involuntary terminations on or after September 1, 2008, through December 31, 2009. Because the law is retroactive, it must address how to deal with employees who were previously terminated.

As noted, the law requires a special 60-day election period for a qualified beneficiary to elect the subsidized coverage. However, the special 60-day election period does not extend the period of COBRA continuation coverage beyond the original maximum required period (generally 18 months after the qualifying event), and any COBRA continuation coverage elected pursuant to this special election period begins on the date of enactment and does not include any period prior to that date.

Reimbursement Procedures

The statute describes the reimbursement procedures for the subsidized COBRA continuation coverage that is not paid by the assistance eligible individual. The statute is very clear as to who is entitled to the government reimbursement. The entity eligible for reimbursement is: (1) the multiemployer plan, if the plan provides the coverage; (2) the employer, if the employer maintains the plan and is subject to federal COBRA or is self insured; or (3) in all other cases (*e.g.*, if the employer is a small employer subject to state or mini-COBRA) the insurance company is eligible for the credit.

Small employers that are insured and not subject to federal COBRA should note that absent additional guidance from the IRS, they *cannot* claim the payroll tax credit—the insurance company must technically take the credit. Thus, if the employer actually pays the full premium to the insurer, the employer will need to work out a method to be

reimbursed by the insurance company for the credit that the insurance company can take.

An entity is not eligible for reimbursement until the entity has received the reduced premium payment from the assistance eligible individual. To the extent that such entity has liability for income tax withholding from wages or FICA taxes with respect to its employees (for example, an employer with a self-insured plan), the entity will receive a credit against its liability for these payroll taxes. If such amount exceeds the amount of the entity's liability for these payroll taxes, the entity will be paid directly. The IRS has already amended its Form 941 so that the entity eligible for the reimbursement can claim the payroll tax credit by reporting the number of covered individuals and the amount of the subsidy to which they were entitled.

Issues Raised by the New Law

Employers, plan administrators, and health plan providers face numerous challenges, in implementing this new law, in addition to the obvious challenge of providing notices and amending health plans.

First, the expansion of the COBRA subsidy to small employers subject to state law requirements may cause significant new "start-up" issues for entities that may have had less sophisticated administrative procedures in place. In addition, because state laws vary and the federal government is not accustomed to dealing with them, it may be difficult for the government to provide small employers with timely guidance.

Second, the eligibility requirements for the subsidy will pose challenges. Although presumably former employees must monitor their own income limits in determining eligibility for the subsidy, some employees will need assistance in estimating their income.

In addition, the employer will have to determine who is terminated "involuntarily." There is no statutory definition or guidance. In some cases, this will be easy; in others, such as "constructive terminations" where responsibilities, salaries, or benefits are reduced and the employee feels he or she has no other choice but to leave, the determination is less clear.

There is a provision for expedited review by the Secretary of Labor or Health and Human Services (in consultation with the Secretary of the Treasury) of denials of the premium subsidy. Under the conference agreement, such reviews must be completed within 15 business days (rather than ten business days as provided in the House bill) after receipt of the individual's application for review. This is an extraordinary new "remedy" that will likely be unworkable in a timely manner.

Finally, the new reimbursement mechanism will present challenges. The conference agreement clarifies that any reimbursement for an amount in excess of the payroll taxes owed is treated in the same manner as a tax refund. Moreover, overstatement of reimbursement is a

payroll tax violation. So, if the employer makes a mistake in implementing this new and confusing law, it can be subject to penalties.

In addition to the DOL Web site described above, other guidance may be found at www.irs.gov and www.cms.hhs.gov.

Changes to SCHIP Rules

One of President Obama's earliest legislative acts was to sign the Children's Health Insurance Program Reauthorization Act of 2009. This Act funds the well-known state children's health insurance program known as SCHIP.

The law contains a new provision that allows states to subsidize certain employer-provided health coverage (but excludes discriminatory plans, high-deductible plans, FSAs, or plans for which the employer pays less than 40 percent of the cost). These subsidies can be paid directly to the employee or to the employer. The employer can opt out of a direct payment from the state, but must allow eligible individuals to enroll. Plans will have to provide notice of premium assistance once the Department of Health and Human Services provides model forms.

Effective April 1, 2009, the law requires special enrollment rights in an employer-provided plan upon loss of SCHIP coverage that may differ from a plan's current enrollment procedures. Plans will have to be amended to reflect these changes. They may also need to make it clear that the plan retains primary coverage over state programs.

Mental Health/Addiction Parity Act

The 1996 Mental Health Parity Act prohibits plans from imposing lower lifetime annual limits on mental health benefits than those limits imposed on other health benefits. The Paul Wellstone and Pete Domenici Mental Health Parity and Addiction Equity Act of 2008 expand the scope of that Act. For plan years beginning on or after October 3, 2009, the new Act applies to plans that cover mental health or substance abuse benefits.

The new law provides that maximum limitations, as well as limits on deductibles and copays, and number of treatment limits, may not be more restrictive for mental health or substance abuse benefits than those imposed for other health care benefits provided under the plan. This includes rules for use of out-of-network providers. Special rules apply to procedures used to demonstrate medical necessity. Employers will want to review plans that provide such benefits to ensure they comply.

Implications

These measures show that, at least until comprehensive health care reform is enacted, Congress will continue to rely on, and regulate, the

employer-provided health care system. Moreover, the addition of subsidies into the equation could result in a “partnership” with the federal government for employers that provide health care. But as the banks and other financial institutions whose operating practices and whose executives’ salaries are being limited if they take certain government assistance, such partnerships with Uncle Sam come at a price.

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