



## STIMULUS LAW MAKES MAJOR CHANGES TO COBRA

On February 17, 2009, President Obama signed into law the American Recovery and Reinvestment Act (H.R. 1). The Act contains significant changes to the Consolidated Omnibus Budget Reconciliation Act (“COBRA”) continuation coverage rules. The key changes are (1) the government will subsidize 65% of the cost of COBRA premiums for eligible individuals, and (2) eligible individuals who were involuntarily terminated since September 2008 will have a second chance to elect COBRA. The changes are generally effective March 1, 2009.

### **Who is eligible?**

An “eligible individual” is an individual (1) whose employment is or was involuntarily terminated between September 1, 2008 and December 31, 2009, and (2) who is otherwise eligible under COBRA for continued coverage under his former employer’s health care plan. The Act does not define “involuntary termination.” It is not clear whether the term includes voluntary terminations for good reason (e.g., the employee quits when the employer requires him to move to another state to perform his job), or terminations in connection with voluntary early retirement programs, or “window” programs designed to reduce an employer’s workforce.

If an individual’s adjusted gross income is less than \$125,000 (\$250,000 if married filing jointly), then the subsidy is fully available. The subsidy is phased out for taxpayers earning more, and individuals earning over \$145,000 (\$290,000 if married filing jointly) will not be eligible for any subsidy.

If an individual is not eligible for the full subsidy because of the income limitation but takes the benefit of the subsidy anyway, he must report the amount of subsidy received as additional tax owed (not merely as additional taxable income) on his income tax return.

Terminated employees of an employer whose plan is not governed by COBRA (due to having fewer than 20 employees) but who reside in states that have “comparable continuation coverage” laws (“mini-COBRA” laws) are eligible for the subsidy, as are terminated governmental employees. It is unclear how the subsidy and special enrollment rights will operate in conjunction with mini-COBRA laws and which states’ laws would be deemed “comparable,” a term not defined in the Act.

### **What is the COBRA subsidy and how is it provided?**

The Act provides that an eligible individual (or someone other than the employer on the individual’s behalf) needs to pay only 35% of the COBRA premium in order to purchase continued health-care coverage. The government will provide the remaining 65% of the COBRA premium charged to the eligible individual for up to nine months, but the employer must pay the 65% up front. The employer is reimbursed by means of a credit against the employer’s payroll tax deposits and/or federal income tax withholding liability, or a refundable credit. It is unclear how the COBRA subsidy and employer tax credit will operate if an employer already subsidizes COBRA premiums.



Perhaps expecting that there will be delays in compliance, Congress provided in the Act that if eligible individuals pay more than 35% of their COBRA premiums in the first two months that they are eligible for the subsidy (such as March or April of 2009), the employer may apply the excess against future premiums owed by the individual or must refund the overpayment (if the credit would not be used up by the individual within 180 days).

### **What rights do individuals have if they did not timely elect COBRA?**

A special enrollment period gives eligible individuals who were terminated on or after September 1, 2008 a second chance to elect COBRA and take advantage of the government subsidy. The special enrollment period begins on February 17, 2009, and ends 60 days after the plan administrator provides the required notice described in the Act.

COBRA coverage under the special enrollment period begins March 1, 2009 in most cases and is not retroactive to the date of the individual's original qualifying event. However, the COBRA coverage period ends in accordance with existing law and is tied to the original COBRA qualifying event (in most cases, 18 months after the qualifying event).

If the employer offers another health plan option that costs the same as or less than the continuation coverage, the employer may allow the subsidy-eligible individual to apply the COBRA subsidy to such optional coverage.

### **How long is the subsidy provided?**

The subsidy is provided for a maximum of nine months. The subsidy ends sooner if the individual becomes *eligible* for coverage under another health plan or Medicare, or if the maximum period of continuation coverage under COBRA expires. If the individual fails to notify the employer that he has become eligible for coverage under another health plan or Medicare, then the individual is subject to a penalty tax of 110% of the subsidy received after he ceased to be eligible.

### **What should employers do now?**

Employers should immediately review the circumstances surrounding recent terminations and identify all former employees who were involuntarily terminated on or after September 1, 2008. Such former employees may be eligible for the subsidy and a "second bite" at COBRA.

Within 60 days of enactment of the Act, the plan administrator must notify any eligible individual under the Act who does not have a COBRA coverage election in effect on February 17, 2009, that the subsidy is available, the requirements for qualification, and provide necessary forms for electing COBRA during the special enrollment period, described above.

The plan administrator must also notify all the eligible individuals who currently have COBRA continuation coverage of the availability of the subsidy and the requirements to qualify for it.

The Act requires the Department of Labor to provide model notices by March 19, 2009 (30 days from enactment), and employers will need to decide whether to wait for the model notices or issue their own forms. Employers who utilize COBRA administrators should contact their service providers to coordinate their response to the Act.



The COBRA provisions in the Act are vague and leave many questions unanswered. Many details of the provisions are not addressed here, and employers should expect further guidance from the DOL, IRS, and their advisors and service providers in the coming weeks.

– *Anita B. Curran and Timothy P. Brechtel*

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*Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, contact:*

Timothy P. Brechtel  
Jones Walker  
201 St. Charles Avenue  
New Orleans, LA 70170-5100  
504.582.8236 *tel*  
504.589.8236 *fax*  
[tbrechtel@joneswalker.com](mailto:tbrechtel@joneswalker.com)

Susan K. Chambers  
Jones Walker  
201 St. Charles Avenue  
New Orleans, LA 70170-5100  
504.582.8394 *tel*  
504.589.8394 *fax*  
[schambers@joneswalker.com](mailto:schambers@joneswalker.com)

Anita B. Curran  
Jones Walker  
201 St. Charles Avenue  
New Orleans, LA 70170-5100  
504.582.8606 *tel*  
504.589.8606 *fax*  
[acurran@joneswalker.com](mailto:acurran@joneswalker.com)

## Employee Benefits, ERISA & Executive Compensation

Blackman, IV, John C.  
Brechtel, Timothy P.  
Chambers, Susan K.  
Curran, Anita B.  
Martin, Edward F.

Murphy, Margaret F.  
Ramelli, Rudolph R.  
Simoneaux, Kelly C.  
Wilson, B. Trevor

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