

## Employee Benefits & Executive Compensation ADVISORY

March 8, 2010

### President Signs Bill That Modifies COBRA Subsidy Rules: Immediate Action Required!

On March 2, 2010, President Obama signed into law the Temporary Extension Act of 2010 (the “Act”). The Act contains several modifications to the COBRA subsidy rules originally included in the American Recovery and Reinvestment Act of 2009 (ARRA) and later modified by the Department of Defense Appropriations Act of 2010 (“Defense Act”). The following is a summary of those key modifications.

#### New Sunset Date

The Act moves the subsidy eligibility sunset date on or before which a qualifying event that is an involuntary termination of employment must occur from February 28, 2010, to March 31, 2010. Election notice procedures and notices should be modified to reflect the new sunset date.

#### Certain Qualified Beneficiaries Whose Initial Qualifying Event Is a Reduction in Hours of Employment Treated as Assistance Eligible Individuals:

Typically, a qualified beneficiary will qualify as an assistance eligible individual (AEI) only if the qualifying event is an involuntary termination of employment occurring prior to the sunset date. However, under the Act, qualified beneficiaries who experience/d a qualifying event that is a reduction in hours of employment occurring anytime on or after September 1, 2008, followed by an involuntary termination of employment between March 2, 2010, and March 31, 2010, qualify as AEIs even though the subsequent involuntary termination of employment is not the qualifying event for COBRA purposes. Although it is not the qualifying event giving rise to COBRA, the Act treats the subsequent involuntary termination of employment as the “qualifying event” for purposes of determining eligibility for the subsidy (and for purposes of identifying the notice due date—see “Notices” below for more information).

This new subsidy rule only applies to periods of coverage beginning after March 2, 2010. Thus, if the COBRA periods typically begin on the first of the month, the first subsidized COBRA coverage period resulting solely from this new rule would begin April 1, 2010.

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**Practice Pointer:** The rule does not operate to extend the qualified beneficiary's COBRA coverage; the COBRA period is still measured based on the original qualifying event that was a reduction in hours of employment. It simply provides a subsidy for any remaining periods of COBRA coverage beginning after that involuntary termination of employment.

**HOWEVER**, it does operate to provide a new election period for those who would be AEIs under this rule but failed to elect or elected and subsequently lost coverage. See "New Election Period" below for more information.

### *Illustration of the new rule:*

1. ABC, Inc. sponsors a group health plan that only covers full-time employees of the company. Prior to January 15, 2010, Bob was a full-time employee of the company and a participant in ABC's group health plan. On January 15, 2010, Bob changes from full-time status to part-time status. Assume for purposes of this illustration that the transition from full-time to part-time status was not a "material negative change" that would otherwise cause the reduction in hours to be treated as an involuntary termination of employment. Under the terms of ABC's plan, Bob's coverage will continue until the end of the month, January 31, 2010, after which he is offered an opportunity to elect 18 months of COBRA. Bob elects COBRA continuation coverage but he must pay 102 percent of the applicable premium since the qualifying event was a reduction in hours of employment and not an involuntary termination of employment. On March 10, Bob is involuntarily terminated from the company due to a reduction in force.

Even though Bob's COBRA qualifying event was a reduction in hours of employment, he is an AEI who may be eligible for up to 15 months of federally subsidized continuation coverage (assuming he is not eligible for other coverage). Since ABC's COBRA coverage periods begin on the first of each month, Bob's first federally subsidized COBRA period will be April 1, 2010 (the first coverage period after the enactment date—March 2).

### **New Election Period**

Individuals who would be an AEI under the new rule described above, but who failed to elect COBRA or elected COBRA and subsequently lost coverage, are entitled to a new election.

### *Illustrations of this rule:*

2. Same facts as Illustration 1 above except that Bob did not elect COBRA continuation coverage following his qualifying event that was a reduction in hours of employment (i.e., transition from full-time to part-time). Bob is now an AEI entitled to a new election.
3. Same facts as Illustration 1 above except that Bob's spouse was also covered under ABC's health plan on the date of the qualifying event. Although Bob chose COBRA, Bob's spouse did not. Bob's spouse is now an AEI entitled to a new election.

**Practice Pointer:** This new rule does *not* operate to give would-be AEIs whose COBRA period has already expired a new COBRA continuation period simply because they have an involuntary termination of employment between March 2 and March 31, 2010.

Although the involuntary termination of employment is treated as the qualifying event for purposes of determining eligibility for the new election and the subsidy, the maximum COBRA period is determined in this instance based on the original qualifying event that was a reduction in hours of employment (e.g., if COBRA is typically measured from the date of the qualifying event, COBRA will be measured here from the date of the reduction in hours of employment). Also, any break in coverage between the reduction in hours and the involuntary termination of employment is not treated as a “break in coverage” for HIPAA portability purposes. Thus, periods of creditable coverage preceding this break must be included on any certificate of creditable coverage otherwise required by HIPAA and applied towards any pre-existing condition exclusion or limitation period.

**Practice Pointer:** This new election period should operate similarly to the special extended election period provided under the original ARRA legislation to those would-be AEIs who experienced an involuntary termination of employment on or after September 1, 2008, and who chose not to elect coverage or elected coverage but lost it prior to February 17, 2009. Thus, the same procedures adopted to comply with that rule should, with appropriate modifications, apply here as well.

This new rule is only applicable for periods of coverage beginning after March 2, 2010. Thus, if the plan typically requires that COBRA continuation coverage be paid for on a calendar month basis, then the date that continuation coverage would begin in this instance is April 1, 2010 (see, e.g., Q-48 of IRS Notice 2009-27). If, however, the plan typically requires COBRA continuation to be paid for on a monthly basis computed from the date coverage is lost, then the coverage start date is not as clear. The date that COBRA coverage would appear to begin in this instance is the first day of the next COBRA period determined as though the qualified beneficiary elected COBRA following the reduction in hours of employment—and not the date that the subsequent involuntary termination of employment occurs. This is because the maximum COBRA period is determined based on the qualifying event that is the reduction in hours of employment.

***Illustration of this rule:***

4. Same facts as Illustration 2 except that ABC typically requires that COBRA continuation coverage be paid for on a monthly basis computed from the date coverage is lost. In this illustration, Bob would have lost coverage on January 15, 2010, and his monthly COBRA periods would run from the 15th of each month through the 14th of the next month. The next COBRA period following Bob’s March 10 termination, if Bob had elected COBRA following the reduction in hours, would begin March 15, 2010. Arguably, this is the date that Bob’s subsidized COBRA continuation coverage would start under this new rule (although the maximum COBRA coverage period would be measured from the date of the reduction in hours of employment in this example).

**Practice Pointer:** Using prior IRS guidance, it would appear that plan sponsors may permit would-be AEs entitled to a new election under this rule to choose a later start date.

## Notices

The same general election rules applicable under ARRA and the Defense Act apply equally to qualified beneficiaries whose qualifying event occurs between March 1, 2010, and March 31, 2010. Election notices should be revised to reflect the new sunset date.

In addition, there are special notice rules for those individuals who are AEs under the Act as a result of a reduction in hours of employment. If those AEs are already receiving COBRA, notice of the new rules must be furnished to such AEs within 60 days of the date of the involuntary termination of employment.

If the would-be AE is not currently enrolled but is entitled to a new election under the Act, then a revised election notice describing the availability of the subsidy (and the corresponding terms and conditions of eligibility) must be furnished within 60 days of the date of the involuntary termination of employment.

Although not specifically stated in the Act, the DOL's reasoning with respect to prior notices suggests that the notice must be furnished without regard to whether the subsequent event is a voluntary or involuntary termination.

**Practice Pointer:** The Act refers to the relevant ARRA provisions to describe the notice contents. Under those ARRA rules, notice of the option to enroll in less expensive coverage, if available, had to be included. Thus, it would appear that the same opportunity may be offered would-be AEs entitled to a new election under the Act.

## Other

- The Act allows the regulators to impose up to a \$110/day penalty on plan sponsors who fail to implement the DOL's/Treasury's determination of eligibility within 10 days after receiving notice of the determination.
- The Act revised the date that the now 15-month subsidy period begins. Under ARRA, the subsidy period began as of the "first of the month" that the COBRA subsidy period applied. Thus, if the first COBRA period to which the subsidy applied was July 15, 2009, through August 14, 2009, the subsidy period was measured from July 1, 2009. The act deletes the "first of the month" language. Therefore, the 15-month COBRA subsidy period will be measured from the first day of the first COBRA coverage period to which the subsidy applies.
- The Act codifies the clarifications made by the DOL in its model notices with respect to the transition period provided under the Defense Act.

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