

LABOR AND EMPLOYMENT ALERT

Subsidies for COBRA Continuation Coverage under the American Recovery and Reinvestment Act

March 2009

On February 17, 2009, President Obama signed into law the American Recovery and Reinvestment Act of 2009 (the "Act"). Among many other things, the Act provides assistance with health insurance premiums to eligible individuals who are involuntarily terminated (referred to as "Assistance Eligible Individuals"). The assistance is provided in the form of a government subsidy to help pay for Consolidated Omnibus Budget Reconciliation Act ("COBRA") coverage should Assistance Eligible Individuals elect coverage. The subsidy, however, is not paid directly to the Assistance Eligible Individual. Rather, the Assistance Eligible Individual's former employer must pay the subsidy and must obtain reimbursement from the federal government through payroll tax credits. The Act, which is retroactive to September 1, 2008, imposes obligations on employers including the reissuance of COBRA notices for individuals who have not been previously advised of the opportunity to receive the subsidy. This Alert summarizes the Act's amendments to COBRA and provides suggestions to assist employers in complying with the Act.

Eligibility and Subsidy

The subsidy provided to each Assistance Eligible Individual is 65% of his or her monthly COBRA premiums for up to nine (9) months, provided the eligible individual timely pays 35% of his or her monthly COBRA premiums. Assistance Eligible Individuals are those who were or are involuntarily terminated between September 1, 2008 and December 31, 2009 and were or are otherwise eligible to receive COBRA benefits. Spouses and children of Assistance Eligible Individuals may also be eligible for the COBRA subsidy. The COBRA subsidy portion of the Act is retroactive in that it permits Assistance Eligible Individuals involuntarily terminated from September 1, 2008 through February 16, 2009 to receive subsidies. At the present time, the COBRA subsidy does not apply to individuals terminated after December 31, 2009.

The subsidy is available to Assistance Eligible Individuals whose modified adjusted gross income is \$125,000 or less (\$250,000 for joint filers) without any tax liability. Assistance Eligible Individuals whose modified adjusted gross income for a taxable year exceeds \$125,000 but does not exceed \$145,000 (\$250,000 and up to \$290,000 in the case of a joint return) may be subject to increased federal tax liability so the government can recover a portion of their COBRA subsidy. Assistance Eligible Individuals whose modified adjusted gross income exceeds \$145,000 (\$290,000 for joint filers) per taxable year must repay as an additional tax, the entire amount of the COBRA subsidy. However, Assistance Eligible Individuals can elect to waive the subsidy, and thereby, avoid taxation issues.

Assistance Eligible Individuals lose the subsidy when they become eligible for certain other group health coverage or Medicare, or if COBRA coverage otherwise ceases.

Reimbursement

Employers obtain reimbursement for the subsidies through a tax credit that they apply to their regular withholdings of federal payroll taxes. Employers must report the amount of the credit on IRS Form 941 and, if requested, may be required to produce documentation demonstrating involuntary terminations and the amount of subsidies paid to Assistance Eligible Individuals.

Notice

Employers are required to provide all Assistance Eligible Individuals with COBRA notice regarding the subsidy and the option to enroll in different coverage (if permitted by the employer). The Act specifies several items which must be included in the notice. (The Act directs the Department of Labor to issue a form of the new notice by March 19, 2009.)

Employers must provide the new notice by April 18, 2009 to all Assistance Eligible Individuals involuntarily terminated prior to February 16, 2009. Eligibility for the subsidy begins at the time of election and continues for up to nine (9) months. Assistance Eligible Individuals remain eligible for COBRA coverage without the subsidy for the remainder of their coverage period (typically eighteen (18) months from the qualifying event). For example, an Assistance Eligible Individual involuntarily terminated on September 1, 2008 who did not elect COBRA coverage, must be provided with a new notice regarding the subsidy by April 18, 2009. If the individual elects coverage on May 1, his or her coverage will cease eighteen (18) months from September 1, 2008 (February 28, 2010), but the individual's right to receive a subsidy will cease nine months from May 1, 2009 (January 31, 2010).

Assistance Eligible Individuals involuntarily terminated from February 17, 2009 through December 31, 2009 must receive the revised notice in accordance with regular COBRA election notice requirements. (Those Assistance Eligible Individuals terminated after February 17, 2009 who received COBRA notices in their pre-Act form must receive a current notice as soon as possible.) Their eligibility for the subsidy begins at the time of their election and continues for up to nine (9) months. Assistance Eligible Individuals remain eligible for COBRA coverage without the subsidy for the remainder of their coverage period.

Employer Compliance with the Act

- Employers should update their COBRA notices to include the provisions required by the Act or contact their legal counsel or their third party administrator to ensure their notice complies with the Act.
- Employers must determine which employees were Assistance Eligible Individuals prior to February 16, 2009 who have not received the updated COBRA notice and issue the new notice to those Assistance

Eligible Individuals by April 18, 2009. Employers must issue the new notice to all other Assistance Eligible Individuals terminated after February 16, 2009 in accordance with COBRA.

- All employment policies and plans should be updated in accordance with the Act's provisions.
- Employers should implement policies and procedures regarding:
 - Reimbursement or credit to Assistance Eligible Individuals who have overpaid their portion of the premium;
 - Reimbursements for the subsidies that will be treated as payroll tax credits and documentation related to those credits;
 - Waiver of the subsidy; and
 - Notification to Assistance Eligible Individuals of the cessation of the subsidy.

Future Lay Offs

The literal language of the Act specifies that an Assistance Eligible Individual is only eligible for the subsidy, and the employer is only eligible for the reimbursement, if the Assistance Eligible Individual (or someone else other than the employer) pays 35% of the COBRA premium. Therefore, employers anticipating a lay off who plan to pay more than 65% of an Assistance Eligible Individual's COBRA premium should consider that they may not be eligible for reimbursement through the payroll tax credit.

Conclusion

The Act creates employer obligations that require immediate attention and careful planning. To avoid penalties and to obtain the full benefit of the tax credit, employers should not delay in implementing new policies and procedures to ensure their compliance with the Act.

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