

# Labor & Employment Advisory

From the Buchanan Ingersoll & Rooney Labor and Employment Group

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## U.S. Department of Labor Issues Model Notices for New COBRA Rules

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The American Recovery and Reinvestment Act of 2009 materially altered the Consolidated Omnibus Budget Reconciliation Act (COBRA) and imposed new rules that will require employers and plan administrators to take certain actions before April 18, 2009. Today, the U.S. Department of Labor (DOL) issued model notices to be used with the new COBRA rules. This advisory briefly summarizes the new rules and comments on how they affect separation pay arrangements.

### COBRA Premium Reduction and Tax Credit

The act gives "assistance eligible individuals" a 65 percent subsidy toward the cost of their COBRA premiums — they will be treated as if they paid the full cost of their COBRA coverage so long as they pay their 35 percent. Employers must front the cost of the 65 percent subsidy, but they can recoup that cost by taking a dollar for dollar credit against their payroll taxes. If the subsidy exceeds their payroll taxes, they can obtain a refund of their payroll taxes.

The employee (or someone acting on behalf of the employee, *other than the employer*) must pay the employee's 35 percent share of the COBRA premium for the employee to receive the subsidy and for the employer to be able to claim the payroll tax credit/refund.

### Assistance Eligible Individual

An "assistance eligible individual" is an employee or a member of his/her family who: (1) is eligible for COBRA coverage at any time between September 1, 2008, and December 31, 2009; (2) as a result of the employee's involuntary termination during that period; and (3) who elects COBRA coverage (when first offered or during the additional election period provided for under the act).

The act does not define the term "involuntary termination." In a set of questions and answers, however, the DOL stated that because an employee terminated for gross misconduct generally is not eligible for COBRA, such a termination generally would not qualify for the employee or the employee's dependents for the subsidy.

### Duration of the Subsidy

The 65 percent subsidy applies to periods of health coverage beginning on or after February 17, 2009, (or March 1, 2009, for plans that charge for COBRA coverage on a monthly basis) and will end upon the *first* of the following to occur: (1) the individual becomes eligible for other group health coverage; (2) when the maximum period of COBRA coverage ends; or (3) after nine months.

Individuals who are paying reduced COBRA premiums must inform their plans if they become eligible for coverage under another group health plan or Medicare. Failure to do so can result in a tax penalty for the individual.

## **Switching Benefit Options**

If an employer offers multiple coverage options to active employees, the employer may, but is not required to, allow assistance eligible individuals to switch their coverage options when they elect COBRA, and allow employees who have already elected COBRA the same opportunity. The additional coverage must have the same or lower premiums as the individual's original coverage and cannot be coverage that provides only dental coverage, vision coverage, a health flexible spending account or coverage for treatment that is furnished in an on-site facility maintained by the employer.

## **Special COBRA Election Opportunity**

Individuals involuntarily terminated from September 1, 2008, through February 16, 2009, who did not elect COBRA when it was first offered, or who did elect COBRA but are no longer enrolled (i.e., because they were unable to continue paying the premium), have a new election opportunity. This new election period ends 60 days after the plan administrator notifies them of their new COBRA rights. COBRA coverage elected during the special election period generally will begin with March 2009.

## **Notice Requirement**

Plan administrators must notify all individuals (not just employees) who experienced or will experience a qualifying event between September 1, 2008, and December 31, 2009, of these new COBRA rules. Additionally, by April 18, 2009, plan administrators must notify all individuals who experienced a qualifying event (not just employees) between September 1, 2008, and February 16, 2009, of these new rules, even if the individual previously rejected or discontinued COBRA coverage.

Today, the DOL issued new model notices that can be used to satisfy these notice obligations. The model notices can be found at <http://www.dol.gov/ebsa/COBRAModelNotice.html>.

There are four new notices: The first, a General Notice (Full Version), is to be sent to individuals who experience a qualifying event between September 1, 2008, and December 31, 2009. The second, a General Notice (Abbreviated Version), may be sent to individuals who experienced a qualifying event since September 1, 2008, and are already receiving COBRA coverage. The third, an Alternative Notice, applies only to certain plans providing continuation coverage under a state law. And the fourth, a Notice In Connection with Extended Election Periods, applies to assistance eligible individuals who experienced a qualifying event between September 1, 2008, and February 16, 2009, and who previously rejected or discontinued COBRA coverage.

## **Expedited Review of Denials of Premium Reduction**

Individuals who request treatment as an assistance eligible individual and are denied eligibility for the 65 percent subsidy may request an expedited review of the dispute by the DOL. The DOL is required to make a determination within 15 business days of receipt of a request for review.

## **Implementing Initial COBRA Reimbursements**

If an assistance eligible individual pays the full COBRA premium for the first two periods to which the 65 percent subsidy applies (generally March and April 2009), the employer must either: (1) reimburse the assistance eligible individual for the 65 percent he or she paid; or (2) provide a comparable credit against future payments.

## **Income Limits**

If an individual's modified adjusted gross income for the tax year in which the premium assistance is received exceeds \$145,000 (or \$290,000 for joint filers), then the amount of the premium reduction during the tax year must be repaid to the U.S. government. 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 reduction that must be repaid is reduced proportionately. Individuals who earn these amounts also have the option to decline the premium subsidy.

## **The Payroll Tax Credit**

Employers can secure a payroll tax credit or payroll tax refund equal to the amount of the 65 percent subsidy the employer provides to assistance eligible individuals. The Internal Revenue Service (IRS) issued new form 941s and

related instructions to explain how to obtain the credit or refund. Among other things, an employer must provide the following information to the IRS:

- Proof that the employees paid their 35 percent of the COBRA premium.
- Proof that the employer paid an insurance carrier for its 65 percent of the COBRA premiums or, in the case of a self insured plan, proof of the premium amount and the fact that the employer provided the coverage.
- An attestation to the involuntary nature of the terminations.

### **How the New Rules Affect Separation Plans and Agreements**

Many separation pay arrangements provide that an employer will pay all or a portion of an employee's COBRA premium. Such arrangements, however, will not permit the employer to claim a tax credit for the 65 percent of the COBRA premium because, as stated above, the employee, or someone acting on the employee's behalf *other than the employer*, must pay the employee's 35 percent share of the COBRA premium for these new rules to apply. Moreover, the new rules undermine an employer's ability to use the payment of COBRA premiums as consideration for a release, at least insofar as the 65 percent the premium the employer is now required to subsidize.

Accordingly, employers and plan administrators must move quickly to implement procedures to comply with these new COBRA rules and to provide the required notices before April 18, 2009. Additionally, employers should reconsider separation pay arrangements given these new COBRA rules.

For more information, email the author(s) at [leadvisory@bipc.com](mailto:leadvisory@bipc.com).

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