

The Economic Stimulus Package Impacts Employers by Enacting Important Changes to COBRA

by Laura J. Fowler, Esq.

Employers are placed in the position of deciding what constitutes an "involuntary termination." When evaluating these and other questionable scenarios, employers need to keep in mind the purpose of ARRA, in general, and the COBRA subsidy, in particular.

The economic stimulus package signed by President Obama on February 17, 2009 – called the American Recovery and Reinvestment Act of 2009 ("ARRA") – includes some important provisions for employers regarding coverage and notice requirements under the federal Consolidated Omnibus Budget Reconciliation Act ("COBRA"). An employer-provided subsidy for continuation health coverage went into effect on March 1, 2009, and employers are grappling with how to apply the rules and ensure that notice requirements are satisfied.

What Is the Subsidy?

COBRA – which applies to employers with twenty or more employees – allows involuntarily terminated employees and their eligible dependents to continue group health benefits coverage for up to eighteen months. Employers are now obligated to provide "assistance eligible individuals" with a subsidy, equal to 65% of the COBRA premium, for up to nine months following an "involuntary termination."

How Do Employees Receive the Subsidy?

As of March 1, 2009, "assistance eligible individuals" are only required to pay 35% of the COBRA premium. Employers (or health plans, if they administer COBRA benefits and receive employee COBRA payments) are required to pay the remaining 65%. Employers or health plans are then reimbursed through a credit on certain employment taxes or, where tax credits do not provide a sufficient basis for recouping the amounts paid, through a direct payment from the Secretary of the Treasury.

Who Is Eligible for the Subsidy?

Individual employees and their eligible dependents who have lost group health coverage as a result of an "involuntary termination" occurring between September 1, 2008, and December 31, 2009, are considered "assistance eligible individuals."

Employees are not eligible for the subsidy if they lost coverage due to a resignation or reduction in hours (even if that reduction in hours was employer-imposed). Employees are also not eligible if they were terminated for "gross misconduct." "Gross misconduct" is not defined by COBRA but is generally understood to mean intentional, wanton, willful, or reckless acts against an employer's interest. When analyzing who is eligible for the newly-enacted subsidy, employers now may focus on whether an employee engaged in "gross

misconduct" sufficient to make him or her ineligible for COBRA. If, however, an employee was initially offered COBRA coverage after September 1, 2008, the employer does not now have the opportunity to revisit whether that employee engaged in "gross misconduct." If an employee was initially offered COBRA coverage post-termination, then the employer must provide the subsidy if the employee is otherwise eligible.

Employees are not eligible for the subsidy if they are or become eligible for Medicare or for coverage under another group health plan (i.e., through a new employer or the plan of a spouse or domestic partner). If an individual must satisfy a waiting period before becoming eligible for new coverage, the subsidy will continue until that waiting period has been satisfied (as long as the maximum subsidy period has not been reached).

ARRA also imposes income threshold limits. Individuals whose modified adjusted gross income for any taxable year exceeds \$145,000 (or \$290,000 for those filing jointly) are not eligible for the subsidy. Individuals whose modified adjusted gross income exceeds \$125,000 (or \$250,000 if filing jointly) are eligible for only a prorated amount of the subsidy. Employers need not assess whether particular individuals are ineligible for the subsidy due to these income limitations. Unless an individual voluntarily opts out because of anticipated income, employers are required to provide the subsidy. An employer that provides the subsidy to an individual who turns out to be ineligible due to income will still be reimbursed. The federal government will recoup the money directly from the ineligible employee through income tax adjustments.

What Are the New Notice Requirements?

ARRA imposes additional notice requirements on employers. Employers must notify employees terminated on or after September 1, 2008, about the premium subsidy. For employers that offer employees a choice of health plans, ARRA permits employers to offer "assistance eligible individuals" the option of switching to a lower cost health plan. This provision, however, is optional. The alternate plan must have a lower cost and actually provide health care benefits (i.e., vision or dental plans, health spending accounts, and medical reimbursement plans do not qualify). If an employer offers a less expensive plan and elects to make it available to those offered COBRA, the employer must notify them of the option to switch to a lower cost plan.

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In addition, ARRA requires employers to send notices to “assistance eligible individuals” who became COBRA eligible between September 1, 2008 and February 16, 2009, and who initially declined or lost COBRA coverage. This notice must advise these individuals that they are eligible for a premium subsidy and have a renewed right to elect COBRA coverage within 60 days from the notice. Employers are required to provide notice within 60 days of ARRA’s enactment (February 17, 2009).

The federal Department of Labor (“DOL”) has issued a variety of “model notices,” which are available on DOL’s website at <http://www.dol.gov/ebsa/COBRAModelNotice.html>. Each notice is designed for a particular group of qualified beneficiaries. Employers should review these notices and the accompanying guidance from DOL and then coordinate with their insurance companies before providing the requisite notices.

When Does the Subsidy End?

The subsidy starts on March 1, 2009 and ends upon the first occurrence of any one of the following: (1) the individual becomes eligible for other group coverage or Medicare; (2) after nine months of receiving a subsidy; or (3) when the maximum period of COBRA coverage ends.

What Is the Impact on Severance Agreements?

Employers sometimes agree to pay COBRA premiums for terminated employees as a condition of severance agreements. For any months in which employers pay or agree to pay COBRA premiums, the employee is not eligible for the subsidy and the employer is not eligible for reimbursement. To be eligible for the subsidy, the employee must pay 35% of the premium. If an employer agrees to pay part of COBRA premiums, employers are only eligible for reimbursement for 65% of the employee-paid portion. The end result is that employers will likely opt not to pay for any COBRA coverage but may opt instead to extend additional monetary severance benefits to terminated employees.

How do ARRA’s Provisions Apply to Cal-COBRA?

Many states, including California, have enacted laws extending COBRA-like benefits to smaller employers. In California, Cal-COBRA applies to employers with 2-19 employees. ARRA specifies that the premium subsidy extends to “assistance eligible individuals” covered by Cal-COBRA. ARRA does not, however, require employers covered by Cal-COBRA to provide a renewed election period, nor does it require employers covered by Cal-COBRA to consider whether to provide employees with a choice of alternate coverage. Employers covered by Cal-COBRA should consult with their insurance companies to coordinate issuing the requisite notice. Employers covered by Cal-COBRA should also consult with their insurance companies before providing any renewed election period or offering employees a choice of alternative coverage.

What About Domestic Partners and Same-Sex Spouses?

Under federal COBRA, eligible dependents include spouses and dependent children. Domestic partners and same-sex spouses are not considered “qualified beneficiaries” under COBRA and are not legally entitled to continued coverage

under a group health plan. An employer, however, can voluntarily extend COBRA coverage to domestic partners and same-sex spouses, as long as doing so is consistent with the terms of the plan.

Under California law, employers with 2 to 19 employees are required to extend Cal-COBRA continuation coverage to registered domestic partners and same sex spouses. While domestic partners and same-sex spouses may be eligible for continued coverage under COBRA (if employers voluntarily opt to do so) or Cal-COBRA, the subsidy does not extend to these individuals because of the federal Defense of Marriage Act (passed in 1996 and codified at 1 U.S.C. § 7 and 28 U.S.C. § 1738C). Employers can voluntarily provide the subsidy to these individuals but will not be reimbursed by the federal government.

What Are the Unanswered Questions?

Notably, ARRA does not define what is meant by “involuntary termination.” There are a few clear points at either end of the spectrum, but many grey areas in between. For example, an employee laid off for lack of work has been involuntarily terminated and is therefore eligible for the COBRA subsidy, while an employee who resigns to accept alternate employment has not been involuntarily terminated and is not eligible. However, what about the employee who accepts a voluntary lay-off package or resigns in anticipation of being targeted in a series of layoffs? Or what about the employee who voluntarily reduces hours to part-time to avoid a layoff? Or the employee who fails to report to work for three consecutive days and is terminated for “job abandonment” under a consistently-enforced employee handbook policy?

Employers are placed in the position of deciding what constitutes an “involuntary termination.” When evaluating these and other questionable scenarios, employers need to keep in mind the purpose of ARRA, in general, and the COBRA subsidy, in particular. The subsidy is intended to assist individuals who have lost their jobs and their healthcare coverage involuntarily. The meaning of the term “involuntary” will become clear only when the Department of Labor issues clarifying regulations or renders rulings on challenges by employees who have been deemed ineligible for the subsidy.

The changes enacted to COBRA provide important rights to employees and impose important obligations on employers. Employers are still waiting for guidance on important questions but are obligated to comply with its terms immediately.

About the Authors

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