

## New Law Requires Immediate Action by Employers and Administrators

On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009 (the "Act"), which includes significant changes relating to premium assistance for continuation coverage to "assistance eligible individuals." As a result of these changes, plan administrators will need to act quickly, in some cases as soon as March 1, to update their systems and to **notify affected individuals of their rights and obligations** under the Act. In addition, payroll departments must coordinate with plan administrators to prepare for **new reporting and disclosure requirements** relating to the employer's payroll tax liabilities.

### Applicable terminology

For these purposes, an "assistance eligible individual" (an "AEI") is defined as any qualified beneficiary who, between September 1, 2008 and December 31, 2009, is eligible for COBRA continuation coverage as a result of a covered employee's involuntary termination of employment during that period and who actually elects the coverage. The term "COBRA", for purposes of the Act, includes continuation coverage provided under the Consolidated Omnibus Budget Reconciliation Act of 1985, the Public Health Service Act and similar laws. Notably, the Act does not define the term "involuntary termination", thereby leaving unanswered whether an employee may receive premium assistance under the Act if, for example, he is or was terminated in connection with a constructive termination (i.e. voluntary termination for "good reason") or his participation in a limited window program.

### Reduced premium payments

Pursuant to the Act, an AEI will be entitled to continuation coverage for any month in which coverage is elected on or after February 17, 2009 if he pays 35% of the applicable COBRA premium otherwise required for such continuation coverage. An AEI may generally take advantage of this premium assistance for nine (9) coverage months; provided, however, that the premium assistance will end earlier if (a) the AEI becomes covered under any other group health plan (other than a plan providing coverage only for dental, vision, counseling or referral services (or a combination of such services), a flexible spending arrangement, or coverage for services or treatments furnished in certain on-site medical facilities maintained by an employer), (b) the AEI becomes eligible for Medicare or (c) the AEI exhausts the maximum period of coverage provided under COBRA.

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If, for the first or second coverage period following the enactment of the Act, an AEI who has not waived the premium assistance makes the full premium payment for continuation coverage under the plan, the employer is required to either reimburse the AEI the excess amount paid or apply such excess amount against future premium payments for continuation coverage. Notwithstanding the foregoing, the employer is required to reimburse the excess amount paid if it is not reasonable to believe that the excess will be applied to reduce future premiums within 180 days of the date on which the premium payment was made.

## **Obligation to notify of ineligibility**

An AEI who becomes ineligible to receive premium assistance under the Act is obligated to notify the plan administrator of such event. The Internal Revenue Service may impose a penalty on any AEI who fails to provide the required notice. The applicable penalty is equal to 110% of the premium assistance received by the ineligible AEI (unless he is able to show that his failure to notify the plan administrator is due to reasonable cause and not willful neglect).

## **Exclusion from taxable income**

No portion of the premium assistance received by an AEI will be included in the AEI's gross income for Federal income tax purposes unless the AEI has modified adjusted gross income over \$125,000 (or \$250,000 in the case of married taxpayers filing jointly) To avoid having amounts included in income for this purpose, these AEIs are permitted to irrevocably waive the premium assistance provided under the Act.

## **Reimbursement to employers**

Employers sponsoring group health plans in which AEI's are enrolled for continuation coverage will be reimbursed for the amount of the applicable COBRA premium (i.e. 65%) not paid by the AEI in accordance with the Act. The reimbursement will be provided in the form of a credit against the employer's payroll taxes. If the amount of the credit exceeds the amount of the employer's payroll tax liability, the amount will be treated as an overpayment of such taxes to be refunded to the employer or credited against the employer's future payroll tax liability. The employer will be required to periodically submit reports to the Secretary of Treasury to attest to the involuntary nature of each AEI's termination and to provide the amount of payroll taxes offset by the premium assistance credit and other information regarding the AEIs receiving such assistance (including such individuals' taxpayer identification numbers and whether such premium assistance was used to purchase single or family coverage).

## **Extended election period**

In addition to the reduction in the premium charged to the AEI for continuation coverage, the Act provides relief for certain individuals who did not previously elect continuation coverage under the plan. Specifically, an individual who had not elected coverage as of February 17, 2009, but who would be an AEI if such election was in effect is permitted to elect continuation coverage. Such election must be made in the 60-day period following the date on which the employer provides notice of this election opportunity. If elected, the continuation coverage will commence with the first period of coverage elected after the Act's date of enactment, but may not extend beyond the maximum period of continuation coverage that would have been required under COBRA if the AEI had elected coverage at the time of the qualifying event.

## **Permissible election changes**

Furthermore, the Act permits an employer to allow AEIs to change their initial coverage option elected at the time of the qualifying event, provided that the new coverage option is an option that is offered to active employees at the time the new election is made. If permitted, the right to make this election must be offered to all AEIs and must not allow any AEI to elect new coverage for dental, vision, counseling or referral services (or a combination of such services), a flexible spending arrangement, or coverage for services or treatments furnished in certain on-site medical facilities maintained by an employer. In addition, the premium for the new coverage elected must be less than or equal to the premium for the initial coverage elected at the time the qualifying event occurred. An election to make a change in the coverage option must be made by the AEI within the 90-day period following the date the employer provides the notice explaining the AEI's right to make such election.

## **Notices and required actions**

The notices required under the Act may be included in revised COBRA notices or be distributed as a supplemental notice to affected individuals. The Department of Labor is expected to provide model notices by March 19, 2009. In the interim, we recommend that employers and plan administrators begin taking, or be prepared to take, the following actions, as applicable:

- Plan administrators should contact the human resources department of the employer to determine which employees have been involuntarily terminated on or after September 1, 2008 (for reasons other than gross misconduct);
- Plan administrators should review their records (or, if applicable, coordinate with their outside COBRA administrators) to determine the qualified beneficiaries who are receiving or would be eligible to receive continuation coverage as a result of each such employee's termination and collect mailing addresses for such individuals;

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- Going forward, human resource departments should notify the plan administrator whether terminations occurring after February 17, 2009 and on or before December 31, 2009 are "involuntary" (for reasons other than gross misconduct);
- Plan administrators should send monthly reports to the payroll department listing the names of the qualified beneficiaries receiving premium assistance, the amount of the premium assistance for each qualified beneficiary and a description of whether such assistance is for single or family coverage; and
- Payroll departments should update the monthly reports provided by the plan administrators with the taxpayer identification numbers of the qualified beneficiaries and should report the amount of the premium assistance provided for the prior period as a credit on their payroll tax returns.

Once the model notices have been published, the plan administrators (or, if applicable, the outside COBRA administrators) should prepare and distribute all applicable notices and elections. While the Act does not include a deadline for distributing the notices describing the premium assistance or election to change coverage options, it does require that the notice describing the extended election period be distributed within 60 days of the date of enactment (i.e. **April 18, 2009**). Failure to timely distribute notices will result in a violation of applicable COBRA requirements and, where applicable, will extend the period during which the AEI is permitted to elect continuation coverage or change his coverage option.

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