

# New COBRA Law Affects Flex Plan Administration

By Rich Glass

Rich Glass is chief compliance officer for Infinisource, Inc. He is a licensed attorney and brings more than 15 years of legal expertise, specializing in benefits, human resources and related regulatory compliance. He has testified before the IRS and has provided comments on regulations issued by several governmental authorities. He is a member of the Health Plan Advisory Panel at Thompson Publishing Group. He is a frequent speaker and author on various benefits, employment law and compliance issues.



On Feb. 17, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009 (ARRA), ushering in changes to COBRA administration for group health plans, including health reimbursement arrangements (HRAs).

The COBRA changes take effect on the first period of coverage following the date ARRA was enacted (that is, March 1 for most plans). The Department of Labor (DOL) issued model notices on March 19. A few weeks later, the Treasury Department issued Notice 2009-27.

There are four major aspects of ARRA that relate to flexible benefit plans:

- 1) COBRA subsidy
- 2) Second COBRA election period
- 3) COBRA plan enrollment option
- 4) Payroll tax recapture for COBRA subsidy

In two separate references (those relating to other group coverage that terminates the subsidy and to coverage available under the plan enrollment option), ARRA introduces a concept of “a flexible spending arrangement” (as defined in section 106(c)(2) of the Internal Revenue Code). This tax code provision applies to all health flexible spending accounts (FSAs) offered under a cafeteria plan and most HRAs, unless the maximum amount of reimbursement reasonably available to a participant is less than 500 percent of the value of the coverage. The maximum amount of reimbursement reasonably available is typically equal to the HRA balance. The value of the HRA coverage is typically the applicable HRA COBRA premium (minus 2 percent).

## COBRA Subsidy

The major change is a 65-percent COBRA subsidy for up to nine months for assistance eligible individuals (AEIs) who had an initial qualifying event on or after Sept. 1, 2008, and on or before Dec. 31, 2009. An AEI must be a qualified beneficiary who meets the following requirements:

- The initial qualifying event must be for involuntary employment termination for reasons other than gross misconduct.
- The subsidy is available to all coverage connected with that qualifying event, including HRAs but excluding health FSAs, which are specifically excluded, and health savings accounts (HSAs), which are not subject to COBRA.
- The qualified beneficiary must elect COBRA or applicable state continuation coverage (both small employer and post-COBRA coverage).

The qualified beneficiary must have had modified adjusted gross income (MAGI) of less than \$125,000, if single, or \$250,000, if married filing jointly, for each tax year in which the subsidy is received. The qualified beneficiary may take the subsidy but if the MAGI exceeds the threshold amounts, the credit will be recaptured on

See **COBRA**, p. 4

## Editorial Advisory Board

**MARIANNA G. DYSON, Esq.**

Miller & Chevalier Chartered  
Washington, D.C.

**RICHARD F. FEDERICO**

Managing Partner, Workplace Innovation  
Trumbull, Conn.

**DAVID R. FULLER, Esq.**

Morgan, Lewis & Bockius LLP  
Washington, D.C.

**RODNEY D. GARCIA**

The Collins Firm  
McLean, Va.

**JERRY E. HOLMES, Esq.**

Morgan, Lewis & Bockius, LLP  
Washington, D.C.

**KAREN KIRKPATRICK**

Infinisource, Inc.  
Coldwater, Mich.

**SUSAN NASH, Esq.**

McDermott Will & Emery  
Chicago, Ill.

**ANDREW SHERMAN**

The Segal Company  
Boston, Mass.

**SUSAN SEITEL**

WFC Resources, Inc..  
Minnetonka, Minn.

**VALERI STEVENS,**

**APM, FLMI, CEBS, APA, EA**  
Main Street Benefits  
Torrance, Calif.

the tax return. For those with a MAGI between \$125,000 and \$145,000 (or between \$250,000 and \$290,000, if married filing jointly), the amount of credit that is recaptured on the tax return is according to a sliding scale.

The term “involuntary termination of employment” is defined as “severance from employment due to the independent exercise of the unilateral authority of the employer to terminate the employment, other than due to the employee’s implicit or explicit request, where the employee was willing and able to continue performing services.”

The subsidy does not extend the normal maximum coverage period of 18 months for employment termination. If an AEI becomes eligible (not enrolled) for other group medical coverage, the subsidy ends. Qualified beneficiaries have an incentive to notify employers when this happens. They are subject to a penalty equal to 110 percent of any subsidy that was provided when they were not eligible, unless there is reasonable cause not due to willful neglect. Such group medical coverage excludes coverage for dental, vision, employee assistance plans (EAPs), on-site clinic services and FSAs under Section 106(c)(2).

In cases in which the new employer funds the annual HRA amount up front and makes it immediately available, the maximum reimbursement benefit might exceed 500 percent of the value of the coverage (that is, the COBRA premium minus 2 percent). Then, the HRA would constitute other group medical coverage and could terminate the COBRA subsidy available from the other employer. More guidance from the IRS would be beneficial.

### **Second COBRA Election Period**

Any qualified beneficiary without an election in effect as of Feb. 17, 2009, can make a second election. This includes individuals who, as of Feb. 17, 2009, are still in their first election period and have not elected yet and those who, as of Feb. 17, 2009, do not have current COBRA coverage because it terminated after it was elected. This is true even for coverages that were already terminated. This election period starts when a new election notice is sent. If these individuals elect COBRA, they become AEIs and coverage dates back to the first coverage period after Feb. 17, 2009, not their original loss of coverage date. The initial payment is due 45 days after the special election is made.

The special election period applies to all coverages previously offered to an AEI that were not in effect on Feb. 17 except for health FSAs.

The period of time between the qualifying event date and the start of COBRA coverage does not count toward the HIPAA 63-day gap in coverage for determining creditable coverage.

### **COBRA Plan Enrollment Option**

Employers may — but are not required to — offer all AEIs a new plan enrollment option, allowing them to change to a less expensive medical plan offered by the employer to active employees. If an employer has only one medical plan option, the plan enrollment option does not apply. The premium reduction would then apply to the different coverage.

---

**Whether an HRA could be offered under the plan enrollment option depends if it is a flexible spending arrangement under Section 106(c)(2). This would depend on how the employer funds the HRA.**

---

The plan enrollment option has a 90-day election period. The option cannot be coverage that provides only dental, vision, EAPs, on-site clinic services or a flexible spending arrangement under Section 106(c)(2).

Whether an HRA could be offered under the plan enrollment option would depend on whether it is a flexible spending arrangement under Section 106(c)(2). This would depend on how the employer funds the HRA, as indicated above.

### **Payroll Tax Recapture for COBRA Subsidy**

The way the subsidy works is that the plan initially absorbs the 65-percent portion of the COBRA premium each month. For plans subject to COBRA that are not multiemployer plans, the employer recaptures that payment by reducing its employment tax deposits (that is, for federal income tax withholding, Social Security and Medicare) and reporting these offsets on a revised Form 941. Two new lines (12a and 12b) have been added to Form 941 for quarterly reporting the amount of COBRA premium assistance payments and the number of subsidy recipients.

The DOL has an expedited time frame of 15 business days for reviewing any subsidy-related complaints made by qualified beneficiaries.

The IRS and DOL regularly issue guidance on their respective Web sites, <http://www.irs.gov> and <http://www.dol.gov/ebsa/cobra.html>. A copy of the model notices is available at <http://www.dol.gov/ebsa/cobramodelnotice.html>. A copy of Notice 2009-27 is available at <http://www.irs.gov/pub/irs-drop/n-09-27.pdf>. 