February 26, 2009 *By:Joshua Zuckerberg and Matthew O. Young*

IMPORTANT AND IMMEDIATE CHANGES TO COBRA

On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009 (the "Act"), which, among other things, provides assistance to terminated employees who are eligible for health care continuation coverage under the Consolidated Omnibus Budget Reconciliation Act of 1985 ("COBRA").

BACKGROUND

Before the Act, COBRA provided that employees and their dependents (collectively "Qualified Beneficiaries") who lost coverage under a group health plan due to a termination of employment, reduction in hours, or another qualifying event, were eligible to elect continuation coverage under COBRA. Such coverage generally lasted 18 months, although coverage could be extended to 36 months under certain circumstances. COBRA permitted employers and health plans (collectively "Employer(s)") to charge Qualified Beneficiaries premiums of up to 102% of cost required of the Employer to provide a Qualified Beneficiary with health care coverage.

THE NEW COBRA SUBSIDY

The Act provides a subsidy to help alleviate the burden of COBRA premium payments for most Qualified Beneficiaries. The subsidy will cover 65% of the premium charged to the Qualified Beneficiary, meaning that the Qualified Beneficiary is only responsible for paying 35% of the original COBRA premium to the Employer. The subsidy applies to all health plans covered by COBRA and to similar health care coverage continuation programs under state laws (e.g. New York's mini-COBRA). Therefore the Act applies to small Employers with under 20 employees.

The subsidy is effective for coverage periods beginning after February 17, 2009 (which generally start in March) and applies to Qualified Beneficiaries who lost coverage due to an involuntary termination of employment between September 1, 2008 and December 31, 2009. The subsidy is on a prospective basis only.

The subsidy is available for a maximum of 9 months. The subsidy may end earlier, for example when the Qualified Beneficiary becomes eligible for coverage under another group health plan or Medicare or the maximum COBRA coverage period ends. A Qualified Beneficiary must inform the Employer when he or she is no longer eligible for COBRA coverage. The Qualified Beneficiary's failure to notify the Employer will result in a penalty tax on the Qualified Beneficiary of 110% of the premium reduction.

In order to qualify for the subsidy, the Qualified Beneficiary must pay the reduced COBRA premium of 35%. The Employer will then receive the subsidy from the federal government, which will cover the remaining 65% of the original COBRA premium. Typically, the subsidy will be a credit against payroll taxes. If the subsidy exceeds the payroll taxes, the federal government will provide funds in cash. The subsidy goes to the entity to which Qualified Beneficiaries pay the COBRA premium (i.e. the employer or the health plan).

INCOME LIMITATIONS

The subsidy begins to phase out starting at incomes of $125,000 for individuals and $250,000 for couples filing jointly and is completely eliminated once incomes exceed $145,000 for individuals and $290,000 for couples filing jointly. Any portion of the subsidy that a Qualified Beneficiary receives but for which he or she is not eligible must be reported on his or her annual income tax return and paid back to the government as additional tax.

Consequently, it appears that Employers may ignore the income thresholds and simply permit every Qualified Beneficiary to pay the reduced COBRA premium. However, Employers must permit individuals to elect not to receive the benefit of the subsidy.

Employer Responsibilities

Employers have to make the benefit of the subsidies available immediately and must refund or credit COBRA premiums paid in excess of the 35% on or after February 17, 2009.

Employers must provide notice to Qualified Beneficiaries of the premium reductions at the time they lose health care coverage as an employee, if before 2010. For those Qualified Beneficiaries who lost health care coverage on or after September 1, 2008, notice must be provided by April 18, 2009. The Department of Labor will provide a model notice by March 17, 2009.

Employers may also permit Qualified Beneficiaries to elect to change their health care coverage to a less expensive coverage option, provided that the Qualified Beneficiaries have 90 days after the date the Employer notifies the Qualified Beneficiary that the Employer is making the health care coverage options available, to make this election. If the Employer allows this option, it must make this election available to active participants as well.

Special Election

If a Qualified Beneficiary would be eligible for the premium reduction under the Act had he or she originally elected COBRA coverage, he or she will have an additional 60 days to make a COBRA election after the date of the required notice. This additional COBRA election will not extend the total period of COBRA coverage from the date of the qualifying event (e.g. if a Qualified Beneficiary experienced an involuntary termination on October 1, 2008, and did not elect COBRA coverage, the Qualified Beneficiary's election of COBRA coverage pursuant to this special election starts the COBRA continuation period as of the date of the election but does not extend COBRA coverage beyond the applicable COBRA coverage period measured as of October 1, 2008).

Additional Guidance

The Act calls for the Secretary of the Treasury to issue regulations which will provide further details on the Act's provisions. Also, as indicated above, the Department of Labor must provide a model notice by March 17.

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The foregoing is merely a discussion of the Act and is not intended to provide legal advice. If you would like to learn more about this topic or how Pryor Cashman LLP can serve your legal needs, please contact Joshua Zuckerberg at (212) 326-0885 or Matthew O. Young at (212) 326-0179.

About the Authors

Joshua Zuckerberg
Partner

Direct Tel: 212-326-0885
Direct Fax: 212-798-6379
jzuckerberg@pryorcashman.com

Joshua Zuckerberg has been with Pryor Cashman since 2000 and became a partner in January 2007. His practice covers the entire spectrum of labor and employment issues. He has extensive experience representing and counseling employers on all matters affecting the workplace, including discrimination, harassment, and disability claims, restrictive covenants, wage and hour issues, and termination and severance practices.

In addition, Mr. Zuckerberg represents employee associations whose membership includes physicians, professors, stage directors and fire officers. Mr. Zuckerberg has developed considerable expertise in arbitration, mediation, collective bargaining, and federal and state litigation.

Mr. Zuckerberg is a 1997 graduate of Brooklyn Law School, where he was a member of the Brooklyn Journal of International Law and the Moot Court Honors Society. He was awarded an Edward V. Sparer Public Interest Law Fellowship.

Matthew O. Young
Associate

Direct Tel: 212-326-0179
Direct Fax: 212-798-6905
myoung@pryorcashman.com

Matthew O. Young is an associate in the Employee Benefits, Executive Compensation and ERISA Group at Pryor Cashman. Matthew's practice includes both qualified and non-qualified deferred compensation plans and employee benefits. He is experienced with plan drafting & modification, determination requests, correction of plan defects, plan interpretations, and general ERISA matters, and is also familiar with COBRA and FMLA.