



## *IRS Issues Guidance Addressing New COBRA Law*

As reported *several* times already:

- Employees involuntarily terminated from September 1, 2008 to December 31, 2009 and their family members will only have to pay 35% of the premium amount (rather than the usual 102%) for up to 9 months to continue group health coverage.
- Employers will pay 65% of the premium amount, then take a payroll tax credit for that amount.
- The employer must offer the same health coverage the individual had at the time of the qualifying event in accordance with COBRA, but may also offer other less expensive health coverage options.
- If the premium assistance is provided to high income individuals, then their income tax will be increased by the amount of the subsidy.
- Employees involuntarily terminated from September 1, 2008 to February 16, 2009 and their family members have a second chance to elect COBRA coverage. Coverage will not be retroactive.
- Updated COBRA election notices must be provided to any qualified beneficiary with any qualifying event from September 1, 2008 to now by **April 18, 2009**. The Department of Labor ("DOL") issued model notices.

On Tuesday, the IRS issued Notice 2009-27 with 58 questions and answers, providing guidance on many issues, including some guidance as to the determination of what constitutes an involuntary termination.

The author's questions remain unanswered. The rules appear to have gotten more complicated.

Here are some highlights:

### **Involuntary Termination**

#### Standard

The determination of whether a termination is involuntary is based on all the facts and circumstances. For example, if a termination is designated as voluntary or as a resignation, but the facts and circumstances indicate that, absent such voluntary termination, the employer would have terminated the employee's services, and that the employee had knowledge that the employee would be terminated, the termination is involuntary.

## Examples

Examples of involuntary termination are:

- a 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 employer's failure to renew a contract at the time the contract expires if the employee was willing and able to execute a new contract providing terms and conditions similar to those in the expiring contract and to continue providing the services;
- termination of employment for cause unless the due to gross misconduct;
- an involuntary reduction to zero hours, such as a lay-off, furlough, or other suspension of employment;
- an employee-initiated termination from employment for good reason due to employer action that causes a material negative change in the employment relationship for the employee;
- retirement if, absent retirement, the employer would have terminated the employee's services and the employee had knowledge that the employee would be terminated;
- resignation as the result of a material change in the geographic location of employment for the employee;
- when the employer takes action to end the individual's employment status;
- a lockout initiated by the employer;
- termination elected by the employee in return for a severance package (a "buy-out") where the employer indicates that after the offer period for the severance package, a certain number of remaining employees in the employee's group will be terminated.

Examples of no involuntary termination are:

- a work stoppage as the result of a strike initiated by employees or their representatives;
- an absence from work due to illness or disability before the employer has taken action to end the individual's employment status;
- an reduction of hours to more than zero.

## Leave of Absence Followed by Termination of Employment

So, is an employee who is on a leave of absence and does not return to work involuntarily terminated? The answer is still unclear.

An involuntary termination includes a 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*. However, involuntary termination includes termination when the employer takes action to end the individual's employment status. Is the employer's changing an individual's status from

“on leave” to “terminated” in its records an “action to end an individual’s employment status”?

### **Assistance Eligible Individual**

*Background About the Delayed Employer Notice Rule:* The maximum COBRA coverage period for a loss of coverage due to a termination of employment is 18 months. The coverage period generally runs from the date of the termination of employment. However, an employer can use the “delayed employer notice rule” which means both the maximum coverage period and the period to notify the plan administrator start with the loss of coverage date rather than the termination of employment date.

According to the IRS, to be entitled to the premium subsidy, not only does the involuntary termination have to occur no later than December 31, 2009, but coverage must be lost no later than December 31, 2009.

If an employer provides health coverage for an involuntarily terminated employee after the involuntary termination on the same terms as for similarly situated active employees and the employer treats the provision of health coverage as deferring the loss of coverage, then for purposes of the premium subsidy, the loss of coverage (and eligibility for COBRA) will be considered to occur when the employer’s provision of health coverage on the same terms as for similarly situated active employees ends. However, if the employer treats the provision of health coverage after the involuntary termination as part of its obligation to provide COBRA coverage for the involuntarily terminated employee, then the loss of coverage will be considered to have occurred as of the date for which the employer begins making the provision of such COBRA coverage.

*Example.* An individual is involuntarily terminated from employment on November 15, 2009. Health coverage in connection with the November 15, 2009, termination of employment would normally end on November 30, 2009. However, the individual is provided with severance benefits that include 6 months of health coverage for which no premium is required, running from December 1, 2009, through May 31, 2010. The employer considers no loss of coverage to have occurred until the 6 months of severance benefits have been exhausted. Under these facts, for purposes of COBRA, the loss of coverage does not occur until May 31, 2010, which is after December 31, 2009. Although the individual’s involuntary termination occurs during the required time period, the beginning of eligibility for COBRA coverage does not. Consequently, the individual cannot become an assistance eligible individual (“AEI”). However, if the employer considered the payment of health coverage during the severance benefits period to be the provision of COBRA coverage on behalf of the involuntarily terminated individual, for purposes of COBRA the loss of coverage would be considered to have occurred on November 30, 2009, and thus the individual could become an AEI.

### **Retiree Health Coverage**

*Background About Retiree Health Coverage:* If the active employee and retiree health plans are separate or if they are the same, but the terms are different for each group, the employer must offer COBRA coverage at the time of retirement. If a person elects retiree health coverage (even if the retiree health coverage only lasts 12 months, for example), when retiree coverage expires, COBRA coverage is not offered. There is an exception for dependents, however, if their retiree health coverage is terminated due to a qualifying event. In this case, they are entitled to COBRA coverage from the date of the qualifying event. For example, a retiree and his wife are covered under the retiree health plan. The retiree dies after having been covered 10 months and the wife is no longer eligible. The wife is entitled to 36 months of COBRA coverage from the date of death. However, if the plan is set up so that she would remain on the plan regardless of her husband's death, COBRA would not rear its ugly head again.

On the other hand, if the plan, benefits, and premiums are the same for active employees and retirees, COBRA does not have to be offered at the time of retirement as there has been no loss of coverage giving rise to a qualifying event. At the end of retiree health coverage when COBRA coverage was not previously offered, COBRA coverage must be offered if the maximum COBRA coverage period has not expired. So, for example, if the retiree coverage lasted 12 months, COBRA coverage should be extended for 6 months (18 minus 12 months).

#### Retiree Coverage Treated As COBRA Coverage for Subsidy Purposes

Retiree health coverage can be treated as COBRA coverage for which the premium subsidy is available, but only if the retiree coverage does not differ from the coverage made available to similarly situated active employees (though the amount charged for the coverage may be higher than that charged to active employees and the retiree coverage may still be eligible for the premium subsidy as long as the charge to retirees does not exceed the maximum amount allowed under COBRA).

#### Retiree Coverage That is Not COBRA Coverage for Subsidy Purposes

If retiree health coverage that is not COBRA coverage is offered at the same time that COBRA coverage is offered, the effect on eligibility for the premium subsidy depends on whether the retiree coverage is offered under the same group health plan as the COBRA coverage or under a different group health plan. If offered under the same group health plan, the offer of the retiree coverage has no effect on an individual's eligibility for the premium subsidy.

If offered under a different group health plan, the offer can affect the individual's eligibility for the premium subsidy. If offered to an individual whose eligibility for COBRA coverage arises in connection with an involuntary termination on or after February 17, 2009, the offer of retiree coverage that is not COBRA coverage under a different group health plan than the one under which COBRA coverage is being offered will render the individual ineligible for the premium subsidy. If offered to someone whose eligibility for COBRA coverage arose on or after September 1, 2008, but before February 17, 2009, the offer will render the individual ineligible for the premium subsidy only if the period

the individual is given for enrolling in the retiree coverage extends to at least February 17, 2009.

## Calculation of Premium Subsidy

### When the Plan Charges Less Than 102% of Premium for Part of the Period

The IRS provided the following examples of how the subsidy works when the employer does not charge 102% of premium for part of the subsidy period:

*Example 1.* The employer requires active employees to pay \$200 per month for health coverage. For involuntarily terminated employees, the severance benefits include continued health coverage at the cost of \$200 per month for 6 months after termination. After the 6-month severance period, the terminated employee must pay \$1,000 per month for the remainder of the COBRA coverage. The employer considers the loss of coverage to occur on the last day coverage is in effect before the severance benefits begin to take effect; that is, the employer considers the 6-month severance period to be part of the terminated employee's COBRA coverage period, during which the employer pays \$800 toward the cost of the terminated employee's COBRA coverage.

For the first 6 months, an AEI is entitled to COBRA coverage upon the timely payment of \$70 (35 percent of \$200); for the next three months, the individual is entitled to COBRA coverage upon the timely payment of \$350 (35 percent of \$1,000). The employer's resulting payroll tax credit is \$130 (65 percent of \$200) for the first 6 months and \$650 (65 percent of \$1,000) for the next three months.

*Example 2.* Same facts as Example 1, except that the employer considers the loss of health coverage and the beginning of the terminated employee's COBRA coverage period to occur at the end of the 6-month severance period. For the first 6 months after termination of employment, the terminated employee is not eligible for COBRA coverage and is not an AEI.

The employee therefore pays \$200 for coverage, and no subsidy applies. The employee elects COBRA coverage at the end of the 6-month period and is an AEI. For the next 9 months, the individual is entitled to COBRA coverage upon the timely payment of \$350 (35 percent of \$1,000).

The employer's resulting payroll tax credit is \$650 (65 percent of \$1,000). For purposes of COBRA, if the plan does not use the delayed employer notice rule, the end of the 18-month maximum required period of COBRA coverage is measured from the date of the individual's involuntary termination (that is, 12 months after the end of the 6-month severance period). If the plan does provide for the delayed employer notice rule, the end of the 18-month maximum required period of COBRA coverage is measured from the date of the loss of coverage (i.e., 24 months after the involuntary termination).

### When the Plan Charged Less Than 102% of Premium, but Increased It for the Entire Period

When the plan previously charged less than the maximum premium and increases the premium and the employer provides a separate taxable payment to the AEI, the premium subsidy applies to the increased premium amount.

*Example 1.* Under a group health plan, 102 percent of the applicable premium for COBRA coverage is \$1,000 per month. Prior to February 17, 2009, the plan charged \$400 per month for COBRA coverage. The plan charges \$1,000 per month for COBRA coverage for periods of coverage beginning March 1, 2009. In addition, beginning March 1, 2009, the employer provides a taxable severance benefit of \$600 per month to employees who are AEIs. The premium subsidy is based on \$1,000 for the coverage beginning March 1, 2009, and thus the individual is entitled to COBRA coverage upon the timely payment of \$350 (35 percent of \$1,000).

*Example 2.* Same facts as Example 1, except that, beginning March 1, 2009, instead of providing a taxable severance benefit, the employer reimburses employees who are AEIs for the \$350 the employees pay for the coverage, and the employer excludes that amount from the employees' gross income under section 106. Consequently, the \$350 is treated as paid by the employer, and, because there is no non-employer payment, the premium subsidy is not available, and no payroll tax credit is available to the employer.

#### Non-Qualified Beneficiaries

*Background About Qualified Beneficiaries:* A qualified beneficiary is the employee, opposite sex spouse, and dependent child covered by the group health plan on the date of the qualifying event. A qualified beneficiary also includes a child who is born to or adopted by the covered employee during the period of COBRA coverage. Subject to the preceding sentence, a qualified beneficiary does not include a spouse or dependent child not covered before the qualifying event and/or added to the coverage during a later enrollment period. A qualified beneficiary does not include a domestic partner.

The premium subsidy does not apply to portions of the premium attributable to COBRA coverage for individuals who are not qualified beneficiaries.

Amounts paid by an AEI for COBRA coverage covering one or more individuals who are AEIs and one or more individuals who are not AEIs are allocated first to the cost of covering AEIs and then to the cost of covering non-AEIs. Thus, if the cost of covering a non-AEI does not add to the cost of covering the AEIs, then the cost of covering the non-AEI is zero, and the premium subsidy applies to the full amount paid for the COBRA coverage. If the cost of covering a non-AEI adds to the cost of covering the AEIs, it is the incremental cost that is ineligible for the premium subsidy.

*Example 1.* An individual and the individual's two dependent children are AEIs and have COBRA coverage. The COBRA coverage also covers an individual who is not an AEI. The amount the plan requires to be paid for COBRA coverage for self-plus-two-or-more-dependents for non-AEIs is \$1,000 per month.

The amount the individual would pay (but for the premium subsidy) for covering the individual and the two children (the AEs) under the COBRA coverage is \$1,000 per month. The additional premium amount for coverage of the individual who is not an AE is \$0 per month. The individual is entitled to apply the premium subsidy to the \$1,000, and is entitled to COBRA coverage upon the timely payment of \$350 (35 percent of \$1,000) for the coverage. The employer's resulting payroll tax credit is \$650 (65 percent of \$1,000).

*Example 2.* Same facts as Example 1, except the individual has only one dependent child, and the plan charges \$800 per month for self-plus-one-dependent COBRA coverage. Although the individual's premium (but for the premium subsidy) would be \$1,000 per month for self-plus-two-or-more-dependents COBRA coverage, the portion of the premium attributable to coverage for the individual and the individual's dependent child (both AEs) is \$800.

The individual is entitled to apply the premium subsidy to the \$800 and is entitled to COBRA coverage upon the timely payment of \$280 (35 percent of \$800) for that portion of the coverage. The amount the individual pays for the non-AE is \$200. The individual's total premium payment is \$480 (\$280 plus \$200). The employer's resulting payroll tax credit is \$520 (65 percent of \$800).

*Example 3.* An individual is an AE and has COBRA coverage. The individual has self-only coverage and pays \$157.50 (35 percent of the \$450 per month charged non-AEs for self-only COBRA coverage). During the premium subsidy period, the plan has an open enrollment period during which it allows active employees and qualified beneficiaries to add spouses and dependents to the health coverage. The individual adds the individual's spouse and dependent child, who were not covered prior to the involuntary termination, to the COBRA coverage. Without regard to the premium subsidy, COBRA coverage for self-plus-two-or-more dependents is \$1,000 per month.

The spouse and the dependent child are not AEs because they were not covered by the plan on the day before the involuntary termination. The amount the individual pays for the spouse and the dependent child is \$550 per month (\$1,000 less \$450). The individual is entitled to the premium subsidy with respect to \$450 per month. Thus, the individual is entitled to COBRA coverage upon the timely payment of \$707.50 (\$550 + \$157.50 which is 35 percent of \$450). The employer's resulting payroll tax credit is \$292.50 (65 percent of \$450).

#### Switch to a More Expensive Benefit Package

*Background About Plan Changes After the Qualifying Event:* If a plan allows similarly situated active employees who have not experienced a qualifying event to change the coverage they are receiving (such as in connection with open enrollment), then the plan must also allow each qualified beneficiary to change the coverage being received on the same terms as the similarly situated active employees.

If, due to this rule, an AEI elects a more expensive benefit package, the premium subsidy applies to that more expensive option.

### **Coverage Eligible for Premium Subsidy**

The premium subsidy is available for any group health plan except a flexible spending arrangement ("FSA"). This includes vision-only or dental-only plans, health reimbursement arrangements ("HRAs"), and "mini-med plans," whether or not the employer pays for a portion of the costs for active employees.

### **Beginning of the Premium Subsidy Period**

If a plan requires that COBRA coverage be paid for based on a calendar month and requires an individual who loses coverage other than on the last day of the month and who wishes to enroll in COBRA coverage to pay a pro-rata portion of the monthly premium for the first partial month of coverage, the first period of coverage to which the premium subsidy applies for an AEI who loses coverage after February 17, 2009 is the individual's first partial month of coverage.

For example, if someone is terminated and loses coverage on February 18, 2009 and does not want to wait until March 1 to enroll under the special enrollment period provisions, the premium subsidy will apply as of February 18, 2009.

### **End of the Premium Subsidy Period**

#### Timing of Eligibility for Other Group Coverage

An AEI who cannot enroll in other group health coverage immediately (e.g., who is in a waiting period) is not considered eligible for coverage under the other group health plan. Therefore, the period of premium subsidy will not end.

For example, if, as of February 17, 2009, an AEI meets the eligibility requirements for coverage under a group health plan maintained by the individual's spouse, but cannot enroll and have coverage take effect immediately, the individual may receive the premium subsidy for periods of coverage until the first date that coverage can take effect under the plan maintained by the spouse's employer.

The premium subsidy is available to an AEI if an AEI was eligible for other group health plan coverage prior to February 17, 2009, but has been unable to enroll in the other group health plan coverage on and after February 17, 2009.

#### Eligibility Under an HRA

Eligibility for coverage under an HRA will end the period of premium subsidy unless the HRA qualifies as an FSA.

An FSA is health coverage under which the maximum amount of reimbursement which is reasonably available to a participant of the coverage is less than 500 percent of the

value of the coverage. For this purpose, the maximum amount of reimbursement which is reasonably available is generally the balance of the HRA and the value of the HRA coverage would generally be the applicable premium for COBRA continuation of the HRA coverage. or Medicare or lose eligibility for COBRA coverage before that date.

### Multiple Involuntary Terminations

An AEI is eligible for up to 9 months of premium subsidy for each involuntary termination.

*Example.* An individual is involuntarily terminated and loses coverage as of April 1, 2009. The individual otherwise meets the requirements for an AEI and is allowed the premium subsidy for COBRA coverage beginning April 1, 2009. On July 1, 2009, the individual ceases to be an AEI because of coverage under a group health plan provided by the employer of the individual's spouse. Subsequently, the individual's spouse is involuntarily terminated, the individual loses coverage as of November 1, 2009, and, at that time, otherwise meets the requirements for being an AEI. The individual is allowed up to 9 months of premium subsidy with respect to the involuntary termination of the individual's spouse.

### **Payments to Carriers**

If the carrier and the employer have agreed that the carrier will collect the premiums directly from the qualified beneficiaries, the carrier is required to treat an AEI paying 35 percent of the premium as having paid the full premium, even before the employer pays the carrier the remaining 65 percent.

### **Recapture of Premium Subsidy**

#### Eligibility

A plan cannot refuse to provide the premium subsidy to an individual because of the individual's income. Even if an AEI's income is high enough that the recapture of the premium subsidy would apply, COBRA coverage must be provided upon payment of 35 percent of the premium unless the individual has notified the plan that the individual has elected the permanent waiver of the premium subsidy (or the period for the premium subsidy has ended).

#### Waiver

An AEI who wants to make a permanent election to waive the right to the premium subsidy makes the election by providing a signed and dated notification (including a reference to "permanent waiver") to the person who is reimbursed for the premium subsidy. If an AEI makes the permanent election to waive the right to the premium subsidy, the individual may not later reverse the election and may not receive the premium subsidy for any future period of COBRA coverage in 2009 or 2010, regardless of modified adjusted gross income in those years.

### **Special Election Period**

### Effective Date

An individual involuntarily terminated during the period from September 1, 2008, through February 17, 2009 who still has an open COBRA coverage election period independent of the new law may elect coverage under special election period and receive and only pay for coverage that starts on the first period of coverage beginning on or after February 17, 2009.

### Timely Payment of the Initial COBRA Premium

The qualified beneficiary's first premium payment will be due 45 days after the date on which the election under the special election period is made for that qualified beneficiary.

### **Text**

For a copy of the Notice, visit: <http://www.irs.gov/pub/irs-drop/n-09-27.pdf>

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