

## Changes to COBRA and Your Group Health Plan New Federal SCHIP Law Will Require Cafeteria and Health Plan Amendments

By Alton L. Knighton, Jr.

Two new pieces of legislation will affect and require a prompt response by employers that maintain group health plans. The American Recovery and Reinvestment Act of 2009 (the "Recovery Act"), commonly referred to as the stimulus bill, was signed on February 17, 2009. The Children's Health Insurance Program Reauthorization Act of 2009 (the "CHIP Act") was signed by President Obama on February 4, 2009.

### RECOVERY ACT

#### COBRA Premium Subsidy

An individual who elects COBRA coverage under a group health plan is generally required to pay a premium for that coverage that is equal to 102% of the premium that would be charged an active employee for comparable coverage (although an employer sometimes chooses to pick up all or part of the COBRA premium). The Recovery Act provides that the federal government will subsidize up to 65% of the COBRA premium for an assistance eligible individual (an "AEI"). An AEI is a qualified beneficiary that meets certain requirements. (A qualified beneficiary, for COBRA purposes, can be a former employee or one of the former employee's family members who had been covered under a group health plan.)

#### Conditions

A qualified beneficiary will be an AEI only if his right to COBRA coverage arose from the involuntary termination of the employment of (1) the qualified beneficiary or (2) an employee of whose family the qualified beneficiary was a member and only if that involuntary termination occurred during the period beginning September 1, 2008 and ending December 31, 2009. The qualified beneficiary must have elected COBRA coverage, and at least 35% of the COBRA premium must be paid by the qualified beneficiary, or on behalf of the qualified beneficiary by someone other than the employer.

The subsidy will not be available if the group health plan is an FSA.

Given that the subsidy will be available only if someone other than the employer pays at least 35% of the premium, an employer that is considering paying the entire premium might be wise to instead impose 35% of the premium on the qualified beneficiary in order to shift 65% of the cost to the federal government.

#### Payment of Subsidy

The COBRA premium subsidy will be effected through a reimbursement to the

*(Continued on page 2)*

employer. The employer will receive this reimbursement through a reduction in the employer's federal payroll taxes (both withholding and FICA taxes, including the employee portion of FICA taxes). To the extent the subsidy exceeds the employer's payroll taxes, the employer will be entitled to a tax refund.

### **Special Election Period**

If a qualified beneficiary would be an AEI but for the fact that he did not elect COBRA coverage when he became eligible, he may be given a second opportunity to elect. The qualified beneficiary may elect COBRA coverage at any time during the 60-day period following the date he receives the notice discussed below. If he makes an election during the 60-day period, he will receive COBRA coverage beginning with the first period of coverage (generally a calendar month) that begins after the Recovery Act was signed. Thus, in most cases, the qualified beneficiary's coverage would start retroactively on March 1, 2009.

### **Notice**

If a qualified beneficiary would be an AEI but for the fact that he has not made a COBRA election and was eligible to make a COBRA election with respect to a group health plan before February 17, 2009, the administrator of the plan must give the qualified beneficiary written notice of the special election period described above. The notice must be given within 60 days after February 17, 2009.

The Recovery Act directs the Department of Labor to prescribe a model notice no later than 30 days after the Recovery Act was signed. The deadline for the employer's notice will not be extended by reason of a delay in the production of the model notice.

### **Duration of Subsidy**

The COBRA premium subsidy with respect to an AEI will not be payable for more than nine months. The subsidy will no longer be payable after the end of his COBRA coverage period (generally 18 months after termination of employment) or after the date that he becomes eligible for coverage under Medicare or another group health plan (other than an FSA or a plan that only provides certain limited types of benefits).

### **Reimbursement of Premiums**

If an AEI pays the full COBRA premium for either of the first two months for which a subsidy is payable with respect to the AEI (March and April, 2009 for most plans), the employer is required to reimburse the AEI for 65% of such premium, either through a direct payment to the AEI or through an appropriate reduction in subsequent COBRA premiums.

### **Taxability of Subsidy**

A COBRA premium subsidy is not included in the gross income of an AEI. If, however, a subsidy is payable with respect to an individual or the individual's spouse or dependent and the individual's modified adjusted gross income exceeds \$145,000 (or \$290,000 if the individual files a joint return), the individual's income tax will be increased by the amount of the subsidy. If the individual's modified adjusted gross income does not exceed the above amount but does exceed \$125,000 (or \$250,000 if the individual files a joint return), a portion of the subsidy will be added to the individual's income tax. In order to avoid this tax treatment, the qualified beneficiary with respect to whom a subsidy would otherwise be payable may permanently waive the right to be treated as an AEI (in which case the employer would not receive the subsidy and would certainly require the qualified beneficiary to pay the full COBRA premium).

### **General COBRA Notices**

An employer that maintains a group health plan will need to revise its normal COBRA notices to reflect the revisions made by the Recovery Act, including the reduction in premiums available to qualified beneficiaries as a result of involuntary terminations of employment.

## **CHIP ACT**

### **Special Enrollment Rights**

An employee or dependent who is eligible for coverage under, but not enrolled in, a group health plan must now be allowed to enroll in the plan outside of the plan's open enrollment periods if (1) coverage of the employee or dependent under a Medicaid plan or a state child health plan is terminated as a result of loss of eligibility or (2) the employee or dependent be-

comes eligible for premium assistance under the group health plan provided by a state pursuant to a Medicaid plan or a state child health plan. The special enrollment will be available only if the employee requests coverage under the group health plan not later than 60 days after the date the coverage referred to in (1) is terminated or the employee or dependent is determined to be eligible for premium assistance. The special enrollment rights become effective April 1, 2009.

The CHIP Act applies to both insured and self-insured plans, including health flexible spending accounts (“FSAs”) under cafeteria plans (125 plans). Cafeteria plans that contain such FSAs arguably need to be amended before April 1, 2009 to permit the special enrollment rights, but we would hope that the IRS will not take this position.

The CHIP Act permits states to offer premium assistance for coverage under group health plans for certain low-income children. The premium assistance cannot be provided with respect to an FSA or a high deductible health plan.

### Disclosure

An employer that maintains a group health plan in a state that provides premium assistance under a Medicaid plan or a state child health plan is required to provide a written notice to each employee informing the employee of potential premium assistance available from the state in which the employee resides. The notice can be provided in connection with an open enrollment or together with the summary plan description for the group health plan.

The CHIP Act directs the Department of Labor and the Department of Health and Human Services to jointly generate state-specific model notices to be used for this purpose. The model notices are to be developed not later than one year after the CHIP Act was signed. Employers will not be required to provide their notices to employees until the model notices have been made available.

Employers are also required to furnish requested information concerning group health plan benefits to states that provide premium assistance in order to assist those states in evaluating the cost-effectiveness of their premium assistance programs.

The Department of Labor may assess a civil penalty of up to \$100 a day against any employer that fails to timely provide the required notice to an employee or to timely furnish requested information to a state.

### CONCLUSION

An employer that maintains a group health plan should promptly determine whether the new rules under the CHIP Act and the Recovery Act necessitate any amendments to the employer’s group health plan or cafeteria plan or any revisions to the employer’s COBRA forms, as well as whether the employer is required to give any notices of special enrollment rights or special COBRA election periods.

This article is only a summary of detailed provisions contained in the two acts. If you have any questions concerning the CHIP Act or the Recovery Act, please call Al Knighton (540-983-7632) or Neil Birkhoff (540-983-7699).



**Alton L. Knighton, Jr.**, a principal in the firm, focuses his practice in the areas of tax-exempt bonds, taxable financings, employee benefits and estate planning.

*Al can be reached at knighton@woodsrogers.com or at 540-983-7632.*

### Woods Rogers Tax Group:

**NEIL V. BIRKHOFF, Chair**  
540.983.7699  
birkhoff@woodsrogers.com

**TALFORD H. KEMPER, JR.**  
540.983.7552  
fkemper@woodsrogers.com

**BRIAN MICHAEL BROWN**  
804.343.5023  
bbrown@woodsrogers.com

**ALTON L. KNIGHTON, JR.**  
540.983.7632  
knighton@woodsrogers.com

**CLAUDE D. CARTER**  
540.983.7588  
ccarter@woodsrogers.com

**J. LEE E. OSBORNE**  
540.983.7516  
losborne@woodsrogers.com

**NICHOLAS C. CONTE**  
540.983.7630  
conte@woodsrogers.com

**ALEXANDER I. SAUNDERS**  
540.983.7607  
saunders@woodsrogers.com

**R. NEAL KEESEE, JR.**  
540.983.7627  
keesee@woodsrogers.com

**CHRISTINE FRENZ UNDERWOOD**  
540.983.7512  
cunderwood@woodsrogers.com

**TALFORD H. KEMPER**  
540.983.7622  
kemper@woodsrogers.com

**JOSHUA C. WYKLE**  
540.983.7562  
jwykle@woodsrogers.com