ERISA ALERT
MARCH 2009

A new COBRA subsidy is in effect as part of the American Recovery and Reinvestment Act of 2009 (the "Stimulus Plan"). Employers must take immediate action to comply with the new law.

Background

Under the so-called COBRA rules,[1] when an employee's coverage under group health plans (i.e., health plans maintained by an employer with at least 20 employees) ends as a result of involuntary termination, the employee and their dependents covered under the health plan generally have the right to elect to continue their health coverage at their own expense. An employer can charge employees and their dependents up to 102% of the applicable premium. Health coverage under the COBRA rules can continue up to 18 months or until the employee becomes covered under another employer's group health plan.

Employers are obligated to deliver detailed notices explaining the rights under COBRA to employees and their dependents who lose health coverage as a result of termination.

The New Law

The Stimulus Plan provides that employees that are involuntarily terminated between September 1, 2008 and December 31, 2009 ("Assistance Eligible Individuals") and their dependents are required to pay only 35% of the COBRA premium. The subsidy is available for nine months, but not beyond the maximum period of coverage under COBRA (generally 18 months from the date of termination). Employers will be entitled to a reimbursement from the Federal government for the difference between the full premium and the 35% paid by the Assistance Eligible Individuals. The IRS will provide further guidance, but generally it will issue the reimbursement as a payroll tax credit to the employer.

Income Limitations: The full subsidy is available only to individuals with modified adjusted gross income of $125,000 ($250,000 for joint filers) or less. The subsidy is phased-out for individuals with modified adjusted gross income in excess of $125,000 ($250,000 for joint filers) and reaches zero for modified adjusted income in excess of $145,000 ($290,000 for joint filers). Increasing the individual's income tax liability recaptures the subsidy. To avoid recapture consequences, Assistance Eligible Individuals can opt out from subsidy eligibility by notifying the administrator of the COBRA health plan.

Second Chance Elections: Assistance Eligible Individuals who had not elected COBRA continuation coverage as of February 17, 2009 have a special 60-day period to elect COBRA coverage. The election period ends 60 days after the individual receives the subsidy notice. The second chance election does not extend the maximum period of COBRA coverage.

Notice Requirements: Employers must notify all individuals who became eligible for COBRA coverage on and after September 1, 2008. The notice must contain information about the availability of the 65% subsidy, the availability of the second chance election, the availability of lower cost health plan options (if any), the obligation of the individual

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to notify the plan of eligibility in another group health plan, and the penalty for failure to do so. The Department of Labor will issue a model notice that employers can use or modify to satisfy the notification requirements of the Stimulus Plan.

Effective Date: The subsidy is effective for COBRA premiums for coverage beginning on or after February 17, 2009. For employers that bill COBRA premiums on a monthly basis, the subsidy will apply for the COBRA premiums due for March 2009. However, employers who are unable to timely modify their COBRA bills for the first period or immediately subsequent period in which the subsidy applies may reimburse the Assistance Eligible Individual or provide a credit on subsequent COBRA premium bills to the individual.

What to do now?

The COBRA subsidy provisions of the Stimulus Plan are effective immediately. At a minimum, employers must identify all Assistance Eligible Individuals and prepare and distribute the notices required by the new law. Employers must also modify the COBRA premium bills for their Assistance Eligible Individuals and inform their payroll personnel about the payroll tax credit that should be taken for the premium reimbursements. In addition, employers should review existing severance arrangements and health plan documents to determine the impact under the new law. Employers who are already subsidizing COBRA premium payments may want to review this practice to be entitled for the payroll tax credit.

This COBRA Alert is one in a series of ERISA and compliance-related alerts. To read past alerts, please visit our website at **www.herrick.com**. For more information on the this alert or other ERISA matters, please contact:

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