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ARNOLD & PORTER LLP

CLIENT ADVISORY

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FEDERAL STIMULUS PROVIDES COBRA PREMIUM SUBSIDY

The American Recovery and Reinvestment Act of 2009 (ARRA), which was signed into law on February 17, 2009, makes significant changes to the health insurance coverage continuation provisions of the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA). The purpose of the changes is to make COBRA premiums more affordable for eligible individuals.

In general, ARRA (i) provides a subsidy equal to 65% of the monthly COBRA premium for eligible individuals for up to nine months, and (ii) provides a special late COBRA election period to allow eligible individuals who originally declined COBRA coverage to elect COBRA in order to benefit from the premium subsidy. Highlights of the COBRA provisions of ARRA are discussed below.

Premium Subsidy: COBRA generally allows "qualified beneficiaries" (i.e., employees, spouses, and dependent children) who lose employer-provided health insurance coverage on account of a termination of employment or other specified "qualifying event" to elect to continue coverage for up to 18 months. Employers generally are allowed to, and normally do, charge a maximum monthly COBRA premium equal to 102% of the employer's cost of providing equivalent coverage to active employees. ARRA seeks to expand the utilization of COBRA by providing a subsidy equal to 65% of the monthly COBRA premium for a period of up to nine months for persons who are eligible for COBRA on account of an involuntary termination of employment during the period beginning September 1, 2008, and ending on December 31, 2009. The subsidy is available for periods of COBRA coverage beginning on and after February 17, 2009 (i.e., March 1, 2009, for plans that charge COBRA premiums on a calendar month basis). Generally, a person's eligibility for the subsidy ends if, during the subsidy period, the person (i) becomes eligible for health coverage under another group health plan or Medicare, or (ii) reaches the end of the maximum period of coverage required under COBRA. Penalties apply to any person who fails to provide notice that he or she is no longer eligible for the subsidy.

Implementation of the Subsidy: The 65% subsidy is implemented through a reduction in the employer's federal payroll taxes. Upon an eligible person's payment to the employer of 35% of the monthly COBRA premium, the employer may claim a credit for the 65% portion on its payroll tax returns (Form 941). In respect of COBRA premiums for March and April 2009, the employer may charge a subsidy-eligible person the full monthly premium for those months, provided that the subsidized 65%

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portion of those monthly premiums is credited against the 35% due from the subsidy-eligible person for future months or is otherwise promptly refunded.

Income Limitations: Availability of the 65% subsidy is subject to income limitations. The subsidy begins to be phased out for taxpayers with a modified adjusted gross income of $125,000 ($250,000 for joint filers), and it is fully phased out for taxpayers with a modified adjusted gross income of $145,000 ($290,000 for joint filers). In the event a person actually receives a subsidy (or a portion of a subsidy) to which he or she is not entitled to because of the income limitations, he or she must repay the subsidy (or portion thereof) in connection with filing his or her individual tax return. In order to avoid income limitation issues, a person is permitted to irrevocably elect to waive the subsidy for all periods.

Second Chance COBRA—Special Late Election Period: ARRA provides persons who were eligible to elect COBRA on account of an involuntary termination of employment that occurred during the period beginning on September 1, 2008, and ending on February 16, 2009, but did not do so (as well as for persons that did so elect COBRA but are no longer enrolled in COBRA) with a second chance to elect COBRA coverage in order to benefit from the 65% subsidy. This special election period begins on February 17, 2009, and ends 60 days after the plan administrator provides notice of the special election opportunity. Any COBRA coverage elected pursuant to the special election period (i) begins with the first period of coverage on or after February 17, 2009 (i.e., it does *not* extend back to the time that the person originally could have elected COBRA), and (ii) has its maximum coverage period based on the date of the event that originally entitled the individual to elect COBRA under COBRA's ordinary election rules (i.e., the maximum COBRA period for coverage elected during the special election period generally ends 18 months after the event that originally triggered the right to initially elect COBRA, not 18 months after the beginning of the special election period).

Notices: The plan administrator must provide notice regarding the COBRA premium subsidy to *all* individuals who had a COBRA "qualifying event" during the period beginning on September 1, 2008, and ending on December 31, 2009—not just those who incurred an involuntary termination of employment. ARRA directs the Secretary of Labor to issue a model notice that may be used for this purpose. Notice of the special COBRA election period must be provided during the 60-day period following February 17, 2009, to all individuals eligible to make the special COBRA election.

Expedited Appeals Process: Any person denied the premium subsidy may file an expedited appeal with the US Department of Labor (DOL). The DOL's decision must be rendered within 15 days.

Election of Less Costly COBRA Coverage: If an employer offers multiple health insurance options to active employees, the employer is permitted to offer subsidy-eligible persons the option to switch their COBRA coverage to one of the employer's other health insurance options so long as the other option has the same or lower premium than the person's original coverage. If the person makes such a switch, the new coverage becomes the person's COBRA coverage.

We hope that you find this brief summary helpful. If you would like more information or assistance in addressing the issues raised in this advisory, please feel free to contact:

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