



FOR YOUR INFORMATION

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News For School and Municipal Clients

COBRA Continuation Premium Subsidy

Public employers, including school districts and other municipalities, have a statutory obligation under both Wisconsin and federal law to allow former employees to continue participation in group health plans following certain designated qualifying events. Typically, this obligation is referred to as an employee's "COBRA rights," based on the acronym for the Consolidated Omnibus Budget Reconciliation Act of 1985. COBRA and related Wisconsin law, generally, require group health plans to give employees and certain members of their families ("qualified beneficiaries") an opportunity to continue their group health coverage for up to 18 months (or up to 36 months in certain situations) upon the occurrence of certain "qualifying events," which would otherwise cause coverage to end. Since the enactment of COBRA in 1985, continued health insurance coverage has been offered, but at the expense of the employees and qualified beneficiaries. However, on February 17, 2009, President Obama signed into law the American Recovery and Reinvestment Act of 2009 ("2009 Recovery Act"), which requires employers to subsidize COBRA's continuation of benefits on a temporary basis for certain employees.

The definition of a qualified beneficiary has not changed with the 2009 Recovery Act. This term continues to be defined as an individual covered by a group health plan on

the day before a qualifying event who is an employee, the employee's spouse, or an employee's dependent child. In certain cases, a retired employee, the retired employee's spouse, and the retired employee's dependent children may also be qualified beneficiaries. Finally, any child born to or placed for adoption with an employee during the period of COBRA coverage is considered a qualified beneficiary.

The 2009 Recovery Act has also not changed the definition of a qualifying event. This term continues to be defined as certain events that would cause an individual to lose health coverage. For employees, qualifying events include: (1) a voluntary or involuntary termination of employment for reasons other than gross misconduct, and (2) a reduction in the number of hours of employment that impacts the employee's eligibility for health insurance. For qualified beneficiaries, qualifying events also include: (1) the employee becoming entitled to Medicare; (2) divorce or legal separation of the employee; (3) death of the employee; and (4) loss of dependent child status under the plan rules.

The 2009 Recovery Act leaves in place the requirement, under COBRA, that employers notify plan administrators of a qualifying event within 30 days after an employee's death,

termination, reduced hours of employment or entitlement to Medicare and that a qualified beneficiary notify the plan administrator of a qualifying event within 60 days after divorce or legal separation or a child's ceasing to be covered as a dependent under plan rules. Furthermore, employers, generally, must send employees and qualified beneficiaries an election notice no later than 14 days after the plan administrator receives notice that a qualifying event has occurred. Then, the employee or qualified beneficiary has 60 days to decide whether to elect COBRA continuation coverage and 45 days after electing coverage to pay the initial premium.

However, under the 2009 Recovery Act, effective March 1, 2009, employers must now pay 65% of the COBRA health insurance premiums for an Assistance Eligible Individual ("AEI"). An AEI is an employee (or a qualified beneficiary associated with an employee) who has been (1) involuntarily terminated (which includes an employee on layoff, but does not include termination for "gross misconduct"); and (2) who is eligible for COBRA continuation between September 1, 2008, and December 31, 2009. In order to qualify for the subsidy, the employee must respond, in writing, to the additional notification (discussed later in this document) indicating a desire to elect COBRA continuation coverage and the employee must pay 35% of the health insurance premiums.

The fact that the employee must have been involuntarily terminated in order to qualify for the subsidy has already raised a number of questions. It is clear that a layoff or non-renewal would constitute an involuntary termination. However, it is not clear whether the 2009 Recovery Act intends to provide the subsidy to employees who accept an early retirement incentive or who resign in lieu of non-renewal or termination.

If an AEI is a high income taxpayer (someone who's adjusted gross income exceeds \$125,000), the AEI's income tax for the tax year shall be increased by the amount of the subsidy received. For a non-high income AEI, the subsidy provided is excluded from his or her gross income. The Internal Revenue Service (IRS) is expected to issue regulations and other guidance, as appropriate and necessary, concerning this portion of the 2009 Recovery Act.

The maximum period for which the COBRA premium subsidy may be provided to an AEI is nine months. An AEI's eligibility for the premium subsidy will end earlier if the AEI becomes eligible for another group health plan, health reimbursement arrangement or health flexible spending arrangement; if the AEI becomes eligible for Medicare; or if the AEI's COBRA continuation period (18 months or 36 months) ends before the nine month period expires.

In response to concerns that COBRA continuation coverage does not allow employees and qualified beneficiaries the opportunity to enroll in less expensive health plans, the 2009 Recovery Act encourages employers, in coordination with their group health plans, to offer different, less expensive, health insurance coverage options to an AEI for the COBRA continuation period. Under the 2009 Recovery Act, this "different coverage" will be treated as COBRA continuation coverage. However, such coverage does not qualify as different coverage if it provides only dental, vision counseling or referral services (or a combination of such services); if it is a health flexible spending arrangement; or if it is coverage that provides benefits for services and treatments furnished in an on-site medical facility maintained by the employer that consists primarily of first aid services, prevention and wellness care, or similar care.

In order to allow employees the opportunity to take advantage of the COBRA premium subsidy and different coverage option, if available, the 2009 Recovery Act provides for a special 60-day extended election period for each employee, who would otherwise be eligible for the subsidy if he or she had elected COBRA continuation coverage upon involuntary termination/layoff, which occurred between September 1, 2008, and December 31, 2009. During the 60-day extended election period, an AEI must respond, in writing, to the additional notification indicating a desire to elect COBRA continuation coverage. However, the extended election period does not extend the period of COBRA continuation coverage beyond the original maximum required period (18 months or 36 months).

The 2009 Recovery Act requires that employers, in coordination with their group health plans, specifically notify employees and qualified beneficiaries about the COBRA premium subsidy and different coverage option, if available. The additional notification requirement may be met either by amending existing notice forms, or by including a separate document with the notice otherwise required by COBRA. The additional notification must include: (1) the forms necessary for establishing eligibility for the subsidy; (2) the name, address, and telephone number needed to contact the plan administrator and any other person maintaining relevant information in connection with the subsidy; (3) a description of the extended election period; (4) a description of the obligation of the employee or qualified beneficiary to notify the plan providing continuation of coverage of eligibility for subsequent coverage under another group health plan or Medicare, and the penalty for failing to do so; (5) a description, displayed in a prominent manner, of the rights of the employee or qualified beneficiary to the subsidy and any conditions on entitlement; and (6) a description of the different coverage

option, if available. The 2009 Recovery Act provides for penalties to be imposed upon employers that fail to provide the additional notice. In March 2009, the U.S. Department of Labor (DOL), along with the IRS and the Department of Health and Human Services (DHHS), will develop and issue a sample additional notification form.

Under the 2009 Recovery Act, each employer (including school districts and other public employers) that pays the 65% portion of the health insurance premiums for each AEI is entitled to reimbursement for such payments. The employer must file a claim for reimbursement with the IRS and an amount equal to the portion of the employer-paid premiums will be credited to the employer against payroll taxes owed by the employer. The IRS is expected to issue regulations and other guidance, as may be necessary or appropriate, to carry out the reimbursement and reporting provisions of the 2009 Recovery Act.

As explained above, in order to qualify as an AEI, for purposes of the 2009 Recovery Act, the employee must have been involuntarily terminated from employment during the specified period of time. However, the involuntary termination must not be for "gross misconduct." The 2009 Recovery Act has not disturbed COBRA's rules that eligibility for COBRA continuation coverage may be denied if an employee is terminated for "gross misconduct." The term "gross misconduct" is not defined in the federal statute or regulations. The DOL has advised that it can be assumed that being fired for most ordinary reasons, such as excessive absences or, generally, poor performance, does not amount to "gross misconduct." Under the Federal Employees Health Benefits Amendments Act of 1988, the law that extends coverage benefits to federal employees, the U.S. Office of Personnel Management defined "gross misconduct" as "a flagrant and extreme transgression of law or established rule of

action for which an employee is separated and concerning which a judicial or administrative finding of gross misconduct has been made.”

“Gross misconduct” under COBRA has been interpreted by the Seventh Circuit Court of Appeals, the federal appeals court that governs federal cases arising out of Wisconsin. The court has advised that COBRA relieves an employer from its obligation to provide continued health care coverage, under the “gross misconduct” exclusion, only in limited circumstances. The court has explained that “gross misconduct” must involve more than negligence or incompetence. An employee’s on-the-job errors, such as failing to keep adequate, up-to-date financial records and neglecting to manage and collect company receivables, is not “gross misconduct.” However, other types of conduct, such as fraud, could arguably be viewed as bad faith malfeasance amounting to “gross misconduct.” In defense of a decision to deny COBRA continuation coverage, the court will require that the employer produce evidence of such misconduct in order to support a decision that “gross misconduct” existed.

Over the years, employers have rarely exercised their right to deny COBRA continuation coverage to employees who have been terminated for “gross misconduct.” This is likely due to the fact that an employer would not have a monetary expense if an employee,

who could have been denied such coverage, accepted COBRA continuation coverage. However, in light of the financial obligation for the subsidy now required as a result of the 2009 Recovery Act, it is anticipated that employers will be more vigilant about applying the “gross misconduct” standard.

The 2009 Recovery Act’s changes to COBRA require employers to engage in the following immediate action to comply with the new obligations: (1) employers should identify individuals eligible for COBRA continuation benefits who were terminated on an involuntary basis on or after September 1, 2008 (even if those employees did not elect COBRA coverage when originally offered to them), as well as the qualified beneficiaries associated with those employees; (2) employers should work with legal counsel and/or health plan administrators to prepare new and/or revised COBRA notices; (3) employers should update their COBRA premium payment methods in order to effectuate the employer’s responsibility for 65% of the premiums; (4) employers should make arrangements to document subsidy payments for purposes of obtaining IRS reimbursement; and (5) employers should determine a process to use to communicate with employees and qualified beneficiaries about the conclusion of the subsidy and the obligations of the employees and qualified beneficiaries, if any, at that time.

If you have any questions regarding this topic, please call any of the following members of the Lathrop & Clark LLP School, Municipal, Labor and Employment Law Team.

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