

## **COMPLIANCE AND RISK MANAGEMENT**

### **COBRA Premium Subsidy Under the ARRA**

The economic stimulus bill passed by Congress, the American Recovery and Reinvestment Act of 2009 (“ARRA”), contained a significant modification of the Consolidated Omnibus Budget Reconciliation Act of 1985 continuation of health coverage requirements (“COBRA”), and was generally effective February 17, 2009. Compliance with ARRA’s COBRA requirements by the Trust and employees of Everett Public Schools (“District”) that administer COBRA is vital to the Trust and the District.

#### **I. Background**

ARRA modified the COBRA continuation coverage requirements to provide a subsidy and a second election opportunity for “assistance eligible individuals” for a period of up to nine months. The general requirements and the Trust’s and the District’s compliance obligations are outlined in this Section I Background.

- A. Who is an assistance eligible individual (“AEI”) under ARRA?
  - 1. The individual must be a COBRA qualified beneficiary (“QB”).
  - 2. The COBRA qualifying event (“QE”) must be “involuntary termination” of employment + loss of Trust health plan coverage. “Involuntary termination” is not defined in ARRA. A QE for this purpose *is not*:
    - (a) A reduction in hours;
    - (b) Voluntary termination; or
    - (c) Aging out of dependent status or loss of coverage due to divorce.
  - 3. QE must occur on or after September 1, 2008, and on or before December 31, 2009.
  - 4. The Individual must have elected COBRA continuation coverage or make a new COBRA election between September 1, 2008, and December 31, 2009.
  - 5. AEIs include those who:
    - (a) Are currently receiving COBRA continuation coverage because of involuntary termination on or after September 1, 2008.
    - (b) Became eligible for COBRA continuation coverage because of involuntary termination on or after September 1, 2008, but did not elect to receive coverage.

- (c) Previously elected COBRA continuation coverage because of involuntary termination on or after September 1, 2008 but are no longer covered (for example, because of nonpayment of premium).

B. What do AEIs receive?

1. AEIs are deemed to have paid their COBRA premium if they pay 35 percent of COBRA premiums otherwise charged to the QB. 65 percent of what the AEI would otherwise be required to pay is subsidized by federal government.
2. A second election right if the AEI is not currently covered but otherwise meets criteria to be an AEI.
3. Subsidized coverage:
  - (a) Begins on March 1, 2009.
  - (b) Ends on the earliest of the following:
    - (i) Nine months after it started.
    - (ii) The end of the COBRA continuation coverage period (18 months).
    - (iii) The individual becomes eligible for coverage under any other group health plan (other than non-core coverage) or eligibility for Medicare.
4. There is a recapture of the subsidy by the federal government for high income individuals (\$145,000 (\$290,000 for a joint return)), and a phase-in of recapture between \$125,000 and \$145,000 (\$250,000 and \$290,000 for a joint return)).
  - (a) High income individuals can waive assistance and must notify District of the election.
  - (b) The District is only obligated to charge full COBRA premium for AEI if District receives waiver, per Internal Revenue Service (“IRS”) guidance.

C. What is required of Trust and District?

1. Determine AEIs,
  - (a) Current AEIs – individuals who are current QBs and who were:
    - (i) involuntarily terminated on or after September 1, 2008,
    - (ii) eligible for COBRA on or after September 1, 2008, and
    - (iii) elected COBRA, which is still in effect.
  - (b) Potential AEIs – individuals who were QBs and who:

- (i) involuntarily terminated employment on or after September 1, 2008, but who did not elect COBRA;
  - (ii) involuntarily terminated employment on or after September 1, 2008, and whose COBRA coverage was terminated early; or
  - (iii) involuntarily terminated employment on or after September 1, 2008, and are within their 60-day election period, but have yet to elect COBRA.
- 2. Provide notice of the subsidy right and second election right.
  - (a) DOL provided model notices on March 19, 2009. The Model notices include: General Notice (Full Version); General Notice (Abbreviated Version); Notice in Connection with Extended Election Periods (available on DOL website or we can provide them to you on request).
  - (b) Customize model DOL Notice in Connection with Extended Election Periods and send it to all *potential AEIs*.  
**Deadline: Send on or before April 18, 2009.**
  - (c) Customize the model DOL General Notice (Abbreviated Version) and send it to all *current AEIs*.  
**Deadline: Send or before April 18, 2009.**
  - (d) Customize model DOL General Notice (Full Version) and send to all QBs who experience a QE at any time from September 1, 2008 through December 31, 2009, regardless of the type of QE.  
**Existing COBRA notices should be replaced with the customized General Notice (Full Version). For QEs that occur on or after January 1, 2010, the District and Trust should revert to the notice used previously.**
- 3. The District is required to pay the Trust 65 percent or what AEI would otherwise be required to pay for COBRA.
- 4. The District will claim amount of subsidy against payroll taxes using Internal Revenue Service Form 941.
  - (a) Line 12(a) - indicate the amount of subsidy claimed.
  - (b) Line 12(b) - place to indicate number of AEIs for whom a subsidy is claimed.
  - (c) Revised Form 941 and instructions available on IRS website (see below).
- 5. District must be prepared to submit the following reports (in such time and in such manner as the IRS requires):

- (a) An attestation of involuntary termination, including the date of the involuntary termination (which must be during the period from September 1, 2008 to December 31, 2009), for each covered employee whose involuntary termination is the basis for eligibility for the subsidy.
  - (b) The amount of the subsidy credit claimed and an estimate of the credit to be claimed for the next reporting period.
  - (c) A record of the SSNs of all covered employees, the amount of the subsidy reimbursed with respect to each covered employee, and whether the subsidy was for 1 individual or 2 or more individuals.
- 6. The District must retain documentation, including:
  - (a) Information on the receipt, including dates and amounts, of the AEIs' 35% share of the premium.
  - (b) Proof of each AEI's eligibility for COBRA coverage at any time during the period from September 1, 2008 to December 31, 2009, and election of COBRA coverage.
  - (c) Other documents necessary to verify the correct amount of reimbursement.
- D. What are the consequences of non-compliance?
  - 1. Failure to implement the subsidy or to offer the second chance COBRA election are COBRA violations (charging a higher premium than permitted for COBRA continuation of coverage and defective COBRA election procedure, respectively).
  - 2. Denials of premium assistance are subject to expedited review by the Department of Health and Human Services in consultation with the Treasury Department.

## **II. Involuntary Termination**

### **A. Involuntary Terminations under the ARRA.**

The ARRA provides that an employee who is eligible for COBRA continuation coverage and who is involuntarily terminated on or after September 1, 2008, through December 31, 2009, is eligible for subsidized COBRA continuation coverage premiums for up to nine months. However, in IRS Notice 2009-27, the IRS provides the following rules:

- 1. An involuntary termination means 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. An involuntary termination may include 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 services.

2. The determination of whether a termination is involuntary is to be **based on all the facts and circumstances**. For example, this means that the designation of a termination by the employer as voluntary or as a resignation is not conclusive if 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.
3. If an employee is terminated due to "gross misconduct" and the District and the Trust invoke the "gross misconduct" exception by not providing COBRA to those terminated employees, then, regardless of the employee's status, the employee is not eligible for COBRA and the ARRA premium reduction.

B. Applying the Notice's Rules on Involuntary Termination to District's Employee Classifications.

1. **Temporary Hire Teachers** – Teachers who are hired pursuant to a Certificated Non-Continuing Employee Contract ("Non-Continuing Contract") for a one-year term and who do not receive a subsequent contract for employment with Everett at the conclusion of the Non-Continuing Contract. Temporary Hire Teachers receive health benefits provided by the Trust during the contract period.

The Trust currently takes the position that Temporary Hire Teachers were not involuntarily terminated because there was no exercise of unilateral authority by the District to terminate employment: the contracting parties agreed at the time they entered into the Non-Continuing Contract that employment would terminate on a specific date without an option to be renewed. However, unique facts and circumstances in any individual case may be sufficient to make the expiration of a Non-Continuing Contract an involuntary termination.

2. **Long-term Substitute Teachers and Temporary Employees** – Long-term Substitute Teachers and Temporary Teachers are those who are employed by the District and given a specific assignment for more than ninety (90) days. If they are given an assignment for ninety (90) days or more, they are eligible for health benefits provided by the Trust. These Long-term Substitute Teachers and Temporary Employees lose health benefits when their full-time assignment is completed, either due to a termination of employment or due to a reduction in hours.

In the case of Long-term Substitute Teachers and Temporary Employees, a reduction of hours that results in the loss of health benefits in most instances would not result in an involuntary termination. The nature of the employment relationship with a Long-term Substitute Teacher or a Temporary Employee requires that there be periods of time during the employment relationship in which fewer hours worked. Therefore, a reduction in hours would likely not constitute a negative change in the employment relationship for the employee and the COBRA subsidy would not apply.

However, if a Long-term Substitute Teacher or Temporary Employee loses health benefits because his or her employment with District is terminated entirely, or because his or her hours are reduced to zero for an extended period of time after the loss of health benefits, the change in the employment relationship should probably be treated as an involuntary termination and the COBRA subsidy would apply.

3. **Employees Terminated Following a Protected Period or Due to Disability** – Employees of Everett (both teacher and non-teacher) who are terminated (1) after the expiration of a protected employment or leave of absence period under the Family Medical Leave Act (“FMLA”) or Washington’s worker’s compensation law; or (2) upon Everett’s determination that they cannot return to work because of their disability or because Everett cannot accommodate a particular disability.

Employees that are terminated by the District while absent from work due to an illness or disability should be classified as an involuntary termination and as eligible for the COBRA subsidy. However, persons who voluntarily resign during these types of leaves (such as mothers voluntarily deciding not to return to work after the birth of a baby) would not be considered to have an involuntary termination.

4. **Retired Employees** - Termination due to retirement will constitute an involuntary termination if the facts and circumstances indicate that, absent retirement, the employer would have terminated the employee, and the employee had knowledge that the employee would be terminated.

For example, if the District implements a reduction in force on or before December 31, 2009, and part of the reduction of force is accomplished through early retirements or similar benefits, employees who accept early retirement or similar benefits may be deemed to be involuntarily terminated. Another example of an involuntary termination would be an employee who is essentially forced to retire by the District (for example, in lieu of being disciplined for poor performance).

### **III. The Trust and Premium Assistance Payments**

Under the ARRA, because the Trust's health coverage is subject to the COBRA continuation provisions in the Internal Revenue Code of 1986 and the Public Health Service Act, and because some of the coverage is not provided by insurance, the federal subsidy is paid to the employer maintaining the plan, which is the District.

In order for the District receive the subsidy, which is a payroll tax<sup>1</sup> credit equal to 65% of the COBRA premium, the District must collect 35% of the COBRA premium from the assistance eligible individual and pay the Trust an amount equal to 65% of the COBRA premium ("Premium Assistance Payments"). Instructions for IRS Form 941 tell the employer to report on line 12a the amount of Premium Assistance Payments it made, including only Premium Assistance Payments made on behalf of assistance eligible individuals who paid their reduced premiums.<sup>2</sup>

The Form 941 makes it clear that the District must make the Premium Assistance Payments to the Trust on or before the date it files its Form 941 in order to take the credit on the Form 941.

Legal References:     American Recovery and Reinvestment Act of 2009 (HR-1) Title III –  
                              Premium Assistance for COBRA Benefits  
                              Internal Revenue Service Notice 2009-27  
                              Internal Revenue Service Form 941

Adopted: April 21, 2009

Revised: June 15, 2009

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<sup>1</sup> "Payroll tax" is defined as income tax withholding, employee FICA withholding, and employer FICA taxes.

<sup>2</sup> Under the ARRA, in payroll tax credit may be claimed until the District recovered 35% of the COBRA premium payment from the assistance eligible individual.