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EBEC Law Update

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**COBRA Premium Subsidy and
Other Compensation and Benefit Provisions in
the American Recovery and Reinvestment Act of 2009**

1. COBRA Premium Subsidy

The American Recovery and Reinvestment Act of 2009, P.L. 111-5 (“ARRA” or the “Act”), which was signed by President Obama on February 17, 2009, includes a temporary nine-month government subsidy of 65% of the COBRA continuation health coverage premiums for employees who are involuntarily terminated prior to 2010. ARRA, Part B, Title III, § 3001. This subsidy will take effect by the first premium period after February 17, 2009, which would generally be March 1, 2009. Title III is also known as the Health Insurance Assistance for Unemployed Act of 2009.

65% Subsidy. The Act provides for a government subsidy (by way of payroll tax credit) of 65% of the premium cost for COBRA continuation health coverage for a nine-month period for “assistance eligible individuals” as defined below, with the participant paying the remaining 35%. ARRA § 3001(a). The subsidy is also available for state COBRA rules (e.g., N.Y. where employers with less than 20 employees who are therefore not covered by COBRA are subject to state mini-COBRA rule). ARRA § 3001(a)(10)(B).

- The 65% and 35% amounts are presumably based on the full premium cost permitted under COBRA, i.e., 102% of the company’s average cost.
- Note that payroll periods of coverage for insurance arrangements (at least for calendar year plans) would generally be calendar months. Thus, the subsidy would presumably go into effect on the first day of the month following the date of enactment (March 1, 2009) or the date of election.

Assistance Eligible Individuals. A participant is eligible for the nine month 65% government subsidy (an “assistance eligible individual”) if: (i) the participant has been involuntarily terminated from employment; (ii) the participant is, by reason of such termination, eligible for COBRA continuation health coverage at any time between September 1, 2008, and December 31, 2009; and (iii) the participant will elect or has elected COBRA continuation coverage. ARRA § 3001(a)(3). References in this

summary to the individual or participant also apply to a spouse or dependent that is eligible for COBRA.

- Involuntary termination is not defined in the statute. Termination for gross misconduct is certainly not included since it is not even a qualifying event under general COBRA rules (Code § 4980B(f)(3)(B)). However, it is not clear, for example, whether constructive termination is included, or whether employee buyouts are included.

Phase-Out of Subsidy for High Income Individuals. The premium subsidy is not available for single filers with adjusted gross income (“AGI”) above \$145,000 or joint filers with AGI in excess of \$290,000. The subsidy is gradually phased-out for single filers with AGI in excess of \$125,000 or joint filers with AGI in excess of \$250,000. Code § 139C, as added by ARRA § 3001(a)(15). High income participants can waive the subsidy, or they would refund such amount on their tax return under § 139C.

Duration of Subsidy. Premium assistance ceases for months of coverage beginning on or after on the earlier of the date: (i) the participant becomes eligible for coverage under another group health plan or Medicare (and there is a penalty for participants who do not alert the prior employer of such new coverage); (ii) nine months after the first day of the first month when premium assistance has begun; (iii) expiration of the regular COBRA period, e.g., because 18 months have elapsed or the participant is not making payments, or (iv) the end of the COBRA period that would have applied if the participant had elected COBRA on the initial termination. ARRA § 3001(a)(2)(A).

- The statutory language regarding the nine-month period contemplates that coverage begins at the beginning of a month, which, as stated above, for calendar year plans would generally be the first of each calendar month.

Election to Change Health Coverage Options. The Act provides a special rule that if the employer has multiple health coverage options, an assistance eligible individual (as defined above) may also elect among the various health insurance options, provided the employer allows such election, and the cost for the elected coverage is not greater than the cost of the prior coverage. Such an election can be made up to 90 days after the notice regarding change in coverage is provided to participants. ARRA § 3001(a)(1)(B)(i).

- Although to be eligible for the COBRA premium subsidy the participant must elect the subsidy (or COBRA generally) within 60 days after the notice is given, nevertheless the Act would allow a subsidy or COBRA coverage previously elected to be changed with respect to the type of coverage within 90 days from notice of such coverage options.

Special Enrollment Opportunity on Enactment of ARRA Until 60 Days After Notice is Given. The Act provides a special COBRA enrollment opportunity for former

participants who did not elect COBRA but would still be covered by COBRA if they had so elected. Such former participants who are assistance eligible individuals (as defined above) may elect, beginning on February 17, 2009 and ending 60 days after the notice is provided, to receive COBRA continuation coverage and subsidy for the remainder of the COBRA period or nine months, whichever is less. ARRA § 3001(a)(4).

- Presumably, such special enrollment opportunity will also apply to an election for a change in coverage within the 90 day period.
- The COBRA continuation coverage cannot extend beyond what would have been the original COBRA period.
- The COBRA election would presumably continue on a non-subsidized basis beyond nine months for the remaining COBRA duration.

Notices of Premium Subsidy and Change in Coverage. Notices of the COBRA premium subsidy and change in coverage option must be provided to all individuals who have become eligible for COBRA coverage between September 1, 2008 and December 31, 2009. ARRA § 3001(a)(7)(A). For COBRA events occurring between September 1, 2008 and February 17, 2009, participants must be provided with the applicable notice within 60 days after February 17, 2009. ARRA § 3001(a)(7)(C). The DOL is directed to issue model notices within 30 days of enactment of the Act. ARRA § 3001(a)(7)(D).

- The premium notice must be provided to all participants who had or will have a qualifying event between Sept. 1, 2008 and Dec. 31, 2009, apparently even if the qualifying event was not a termination of employment. See, DOL Fact Sheet: COBRA Premium Reduction (Feb. 26, 2009). Notice should not be required with respect to participants who have not had a COBRA qualifying event during this time period.

Premium Reimbursement. The 65% government subsidy is paid to the employer for self-insured plans or insured plans subject to Federal COBRA, by payroll withholding tax credits. Code § 6432(b) & (c) added by ARRA § 3001(a)(12). Reimbursement of the 65% is only provided once the participant has paid the 35%. Code § 6432(c)(3). The Act allows plans to charge eligible individuals the full COBRA premium for up to two billing cycles following February 17, 2009, provided the plan provides such individuals with reimbursement of the overcharge or a credit for subsequent billing periods. ARRA § 3001(a)(12)(E).

Treatment of Employer Subsidized COBRA. The Act does not address cases where the employer subsidizes part of the COBRA premiums, e.g., as part of a separation agreement.

- It would appear that with employer-subsidized COBRA the employee should be required to pay 35% of the non-subsidized portion, and the

government reimbursement should apply to only 65% of the non-subsidized portion. If the employer pays all the premiums, the participant would not be entitled to any subsidy.

Action Items. Employers and plan administrators should take the following actions:

(i) provide notices to: (A) employees who were involuntarily terminated after August 31, 2008 but did not elect COBRA and would still be on COBRA if they had timely elected it, regarding the premium subsidy and change in coverage elections; (B) employees currently on COBRA, of their rights to a premium subsidy; and (C) update general COBRA notices for the remainder of 2009, if necessary not to be inconsistent with the Act;

(ii) have in place the reduced 35% COBRA premium rate for involuntarily terminations in no event later than the third billing cycle after the February 17, 2009;

(iii) consider notifying all participants of the COBRA premium subsidy for 2009;

(iv) review separation or other related agreements that provide for employer-paid COBRA; it may in many cases be advisable to eliminate the employer subsidy for terminations occurring in 2009; and

(v) prepare for various notice or reporting obligations under ARRA or future guidance.

2. Other Employee Benefit Provisions in ARRA

The Act contains certain other employee benefit related provisions, including the following:

Transportation Fringe. The transportation fringe for transit passes and van-pooling under Code § 132(f) is increased for 2009 and 2010 from \$120 to \$230 a month. ARRA § 1151.

Health Coverage Tax Credit. For 2009 and 2010 the individual health coverage tax credit is increased from 65% to 80% of premiums, and also includes family members even after divorce, death or Medicare for a two year period. Code §§ 35(a) & (g); ARRA §§ 1899A & 1899E.

3. Executive Compensation Revisions of EESA for TARP Recipients

The Act in § 7001 expands the restrictions on compensation for executives of companies receiving assistance under the Troubled Asset Relief Program (“TARP”) under § 111 the Emergency Economic Stabilization Act of 2008 (“EESA”), including the following:

\$500,00 Limit for Top 5 Executives. The \$500,000 limit on deductible compensation under Code §162(m)(5) on the top five senior executive officers, which under EESA was only for certain TARP recipients (those with TARP assets in excess of \$300 million, although in operation Treasury broadened its application), is now expanded to all TARP recipients. ARRA § 7001 amending EESA § 111(b)(1).

Bonuses and Incentive Compensation to Top 25 Employees Only Allowed for Certain Restricted Stock. Bonuses, retention payments or incentive compensation cannot be paid to the top five senior executive officers and up to 20 other most highly compensated employees (depending on level of TARP assistance), except for long-term restricted stock of up to one-third of total annual compensation, provided such restricted stock does not vest until all TARP obligations are repaid. ARRA § 7001 amending EESA § 111(b)(3)(D).

Clawback of Bonuses and Incentive Compensation of Top 25 Employees Where Payments Due to Materially Inaccurate Financial Statements. The top 25 most highly compensated employees of a TARP recipient are subject to a recovery (clawback) of bonuses, retention payments or incentive compensation if these payments have been made based on materially inaccurate financial statements. ARRA § 7001 amending EESA § 111(b)(3)(B).

No Severance to Top 10 Employees. No severance of any kind (not just golden parachutes) may be paid to the top 10 executives if terminated from companies receiving TARP assistance, except for payments for services performed or benefits accrued. ARRA § 7001 amending EESA §§ 111(a)(2) & 111(b)(3)(C).

Independent Compensation Committee. A TARP recipient must establish a compensation committee composed entirely of independent board directors, meeting at least twice a year to evaluate employee compensation plans in light of risk posed to the TARP recipients from such plans. ARRA § 7009 amending EESA § 111(c).

Say on Pay. TARP recipients’ annual proxies must have a separate vote on the executives’ compensation (say on pay), but the vote outcome will not override action of the Board and will not subject the Board to additional fiduciary duties. ARRA § 7001 amending EESA § 111(e).