

Further Details on New COBRA Rules

February 24, 2009

The new COBRA provisions under the Obama economic stimulus plan continue to draw the attention of the employee benefits and payroll administration community. The purpose of this LawFlash is to briefly discuss two evolving interpretations.

Brief Overview

The new COBRA provisions create a 65% federal assistance payment for individuals whose employment is involuntarily terminated on or after September 1, 2008 and through December 31, 2009. The assistance payment can run for up to nine months.

The new COBRA provisions require significant COBRA notice changes, payroll deposit changes to reimburse the assistance payment, and even “second chance” COBRA elections for certain individuals.

The new COBRA provisions are effective immediately and will require major changes for employers, COBRA administrators, and payroll administrators.

A more detailed discussion of these provisions can be found in our February 17, 2009 LawFlash (available at http://morganlewis.com/pubs/EconoStimulus_COBRAAction_LF_17feb09.pdf).

Evolving Interpretations

First, it is becoming increasingly clear that any existing employer subsidy associated with COBRA premiums for involuntarily terminated employees is not eligible for the 65% assistance payment. Such employer subsidies are usually offered as part of an employer’s severance plan and can provide COBRA coverage that is free, equal to active employee rates, or in some other fashion less expensive than the full COBRA rate.

However, the new COBRA 65% assistance payment is only meant to make COBRA premiums less expensive for eligible individuals—not to automatically shift the cost of an existing employer subsidy to the federal government. Thus, in order to take full advantage of the new 65% assistance payment, employers are carefully evaluating whether they should eliminate any employer subsidy for employees who become entitled to COBRA due to an involuntary termination of employment.

Next, with respect to former employees whose income level exceeds the COBRA 65% assistance payment phase-out, it is now apparent that these individuals will have their income tax increased by the amount of any assistance payments they receive under the new COBRA rules. While this will still result in an interest-free loan to the individual until their subsequent income tax filing deadline, some may choose to opt out of the 65% assistance payment. The Secretary of Treasury is expected to issue guidance regarding the form and manner of the opt-out election.

For a broader discussion of these and other issues, please contact any of the Morgan Lewis attorneys listed below:

Chicago

David Ackerman	312.324.1170	dackerman@morganlewis.com
Andy R. Anderson	312.324.1177	aanderson@morganlewis.com
Brian D. Hector	312.324.1160	bhector@morganlewis.com

Dallas

Patti J. Hedgpeth	214.466.4132	phedgpeth@morganlewis.com
Riva T. Johnson	214.466.4107	riva.johnson@morganlewis.com
John A. Kober	214.466.4105	jkober@morganlewis.com
Heath A. Miller	214.466.4118	hmiller@morganlewis.com
Erin Turley	214.466.4108	eturley@morganlewis.com

New York

Craig A. Bitman	212.309.7190	cbitman@morganlewis.com
Gary S. Rothstein	212.309.6360	grothstein@morganlewis.com

Palo Alto

S. James DiBernardo	650.843.7560	jdibernardo@morganlewis.com
Zaitun Poonja	650.843.7540	zpoonja@morganlewis.com

Philadelphia

Robert L. Abramowitz	215.963.4811	rabramowitz@morganlewis.com
I. Lee Falk	215.963.5616	ilfalk@morganlewis.com
Amy Pocino Kelly	215.963.5042	akelly@morganlewis.com
Robert J. Lichtenstein	215.963.5726	rlichtenstein@morganlewis.com
Joseph E. Ronan, Jr.	215.963.5793	jronan@morganlewis.com
Steven D. Spencer	215.963.5714	sspencer@morganlewis.com
Mims Maynard Zabriskie	215.963.5036	mzabriskie@morganlewis.com
David B. Zelikoff	215.963.5360	dzelikoff@morganlewis.com

Pittsburgh

John G. Ferreira	412.560.3350	jferreira@morganlewis.com
Lauren Bradbury Licastro	412.560.3383	llicastro@morganlewis.com
R. Randall Tracht	412.560.3352	rtracht@morganlewis.com

Washington, D.C.

Jessica R. Bernanke	202.739.5447	jbernanke@morganlewis.com
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Althea R. Day	202.739.5366	aday@morganlewis.com
Benjamin I. Delancy	202.739.5608	bdelancy@morganlewis.com
David R. Fuller	202.739.5990	dfuller@morganlewis.com
Mary B. (Handy) Hevener	202.739.5982	mhevener@morganlewis.com
Dean R. Morley	202.739.5989	dmorley@morganlewis.com
Gregory L. Needles	202.739.5448	gneedles@morganlewis.com

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