

Rosen Seymour Shapss Martin & Company LLP

Certified Public Accountants & Profitability Consultants

RSSM Tax Alert

COBRA Subsidy Provisions

Part 4 of 4

Dear Clients and Friends of our Firm:

Among the provisions of the new stimulus package (the "American Recovery and Reinvestment Act of 2009") recently signed by President Obama are subsidies for unemployed workers continuing their health care benefits through COBRA. Here is what you need to know right now about this package:

Background. Under COBRA (the commonly used acronym for the Consolidated Omnibus Budget Reconciliation Act of 1985), most workers laid off from a company that has more than 20 employees and provides health benefits are allowed to keep those benefits for up to 18 months. But until the recent legislation, doing so was forbiddingly expensive because the out-of-work employee had to pay up to 102% of the premiums, often amounting to hundreds of dollars a month for individuals and perhaps a thousand dollars a month for families.

New law. The new stimulus package makes it easier and relatively less expensive for the newly unemployed to obtain health coverage by providing a 65% government subsidy of COBRA premiums for nine months to employees within certain income limits who are involuntarily terminated between Sept. 1, 2008 and Dec. 31, 2009.

Who is eligible for the subsidy. Employees entitled to the subsidy must have been involuntarily terminated (for reasons other than gross misconduct) between Sept. 1, 2008 and Dec. 31, 2009 and must be eligible for COBRA. Employees who voluntarily resign are not eligible for the subsidy.

Although the subsidy applies to employees who were terminated as long ago as Sept. 1, 2008, it is not retroactive. It applies only to periods of coverage (generally months) beginning on or after March 1, 2009. A special election period exists for individuals involuntarily terminated on or after Sept. 1, 2008 who had not elected COBRA. They are given an additional 60 days after they receive notice of the special election period to elect to take advantage of the subsidy.

A terminated employee must pay 35% of the COBRA premium in order to qualify for the federal subsidy. The base amount that is used to calculate the employee's reduced COBRA premium under the Act is the premium that the employee would have been required to pay for COBRA continuation coverage under pre-Act law, generally 102% of

the employer's premium.

Amount of the subsidy. The subsidy will cover 65% of the monthly COBRA premium, for a period of up to nine months.

Eligible employees with modified adjusted gross income of \$125,000 or less (\$250,000 or less if married filing jointly) for the tax year qualify for the full 65% subsidy. For taxpayers with incomes greater than those amounts, the subsidy is phased out through additional taxation until the subsidy is fully recaptured at modified AGI of \$145,000 (\$290,000 for joint returns). However, taxpayers reaching these thresholds can permanently waive their right to a subsidy to avoid this issue and simply pay the full COBRA premium charged.

Duration of the subsidy. Eligible employees may receive a 65% subsidy toward their health care premium for a period of up to nine months beginning on the later of March 1, 2009, or the date the individual loses regular coverage under the plan. That means, for example, that an individual whose COBRA coverage began on Jan. 1, 2009 would be eligible for a subsidy for the nine-month period beginning on March 1, 2009. However, the subsidy will terminate before the end of the nine-month period if (a) the employee becomes eligible for other employer health coverage, (b) the employee becomes eligible for Medicare, (c) the maximum COBRA coverage period required by law expires, or (d) for those electing COBRA during the special election period, the COBRA period starting from the initial time period when the employee could have elected COBRA expires. A former employee who does not notify the employer of (a) or (b) above is subject to a penalty of 110% of the subsidy.

Level of coverage to which the subsidy applies. The subsidy applies to whatever level of COBRA coverage the terminated employee elects. If the employer allows, employees may elect coverage different than that in effect at the time of termination, so long as the premium for that option is no higher than the premium for the pre-termination option. The advantage of this provision is that it allows a terminated employee to switch into a lower-cost health plan, like a health maintenance organization, if the former employer offers one, even if the employee was signed up for a more expensive plan while he was working.

The subsidy isn't taxable income to the terminated employee. A taxpayer's receipt of the subsidy for COBRA continuation coverage is not subject to federal income tax. Further, despite any other provision of law to the contrary, the subsidy may not be considered as income or resources in determining the recipient's eligibility for, or the amount of, any public benefits provided under federal or state law, including that of any political subdivision.

Eligible individual receiving COBRA premium assistance can't claim the health coverage tax credit. To help taxpayers cope with the loss of their jobs due to increased imports from, or a shift in production to, foreign countries, the Trade Act of 1974 (as amended) provides certain benefits, such as job development or referrals. In addition, the 2002 Trade Act provides for a refundable tax credit (the Health Coverage Tax Credit, or HCTC) of 65% of the amount paid for these taxpayers' coverage and that of qualifying family members under COBRA continuation coverage and various state-based group

health coverage.

Under the new law, to prevent double benefits, a taxpayer receiving the premium reduction subsidy for COBRA continuation coverage is not eligible for the HCTC or advance payment of the HCTC.

Mechanics of the subsidy. A terminated employee (or someone other than the employer) must pay 35% of the COBRA premium in order to qualify for the federal subsidy (an employer must actually collect this 35% before requesting reimbursement of the other 65% from the federal government). The remaining 65% of the premium (i.e., the "subsidy") is initially paid by the employer sponsoring the plan under which the COBRA coverage is provided. (In the case of a multiemployer plan, the subsidy is borne initially by the plan.) The employer or plan then obtains reimbursement by taking a credit against its liability to deposit payroll taxes and federal income taxes withheld from the quarterly employees' compensation. If the credit is greater than its quarterly liability, the excess can either be credited against the subsequent quarter or refunded.

Since employers may not be able to implement this premium subsidy in time to meet the March 1 effective date, the Act provides that subsidy-eligible individuals who pay the full COBRA premium for either March or April coverage must either have the 65% subsidy amount refunded to them by the plan's sponsoring employer or have the subsidy credited against their future COBRA premiums.

New notice requirements. An employer is required to notify any eligible employee that was involuntarily terminated between September 1, 2008 and December 31, 2009. The employer can modify its current qualifying event forms or provide the notification as a separate document.

The additional information that must be provided includes:

- any forms necessary for establishing eligibility for the premium subsidy;
- the name, address and telephone number of the plan administrator;
- a description of the second election period;
- a description of the obligation of the eligible employee to notify the plan of eligibility for subsequent coverage under another group health plan or Medicare;
- a description of the eligible employee's right to a reduced premium;
- if available, a description of the option to enroll in lower cost coverage.

For eligible employees terminated between September 1, 2008 and February 16, 2009 who are currently on COBRA, the employer must notify them of these additional rights within 60 days of February 17, 2009. This includes any employee that did not elect COBRA or those that elected COBRA and then subsequently dropped the coverage.

For employees terminated between September 1, 2008 and February 16, 2009, the employer must notify them of these additional rights (except for the second election). This can be done by revising and sending their current election notice or sending them a separate notice.

For employees who experience an involuntary termination between February 17, 2009

and December 31, 2009, the employer should revise the current election notices to include the new provisions or provide a separate notice at the time of the qualifying event.

The Department of Labor will issue model notices no later than March 19, 2009 for the required additional notification.

We hope you find this information helpful. If you would like more details about this or any other aspect of the new law, please feel free to contact us at 212-303-1800 or e-mail us at info@rssmcpa.com. Please visit our website at www.rssmcpa.com.

Sincerely,

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RSSM ANNOUNCES THE ADDITION OF MILLER, ELLIN & COMPANY, LLP

Rosen Seymour Shapss Martin & Company LLP and Miller, Ellin & Company, LLP are pleased to announce the joining of their practices effective January 1, 2009. The firm will operate under the name Rosen Seymour Shapss Martin & Company LLP. The merger adds almost 40 additional personnel including 5 partners and 2 principals.

New Partners

Michael Bernstein, CPA
Bernard P. Lewites, CPA
David W. Ostrow, CPA
Mitchell J. Rubin, CPA
Hilton L. Sokol, CPA, LLM

New Principals

Mark C. Peltz, LLM
Keith B. Stone, CPA

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