

Manage Complexities, Help Avoid Penalties

An Employer's Guide to COBRA

The recent ruling by the Supreme Court of the United States upholding the Health Care Reform Act does not affect an employer's obligation to offer COBRA continuation health care coverage to qualified beneficiaries. In March 2012, the IRS issued revised guidelines for COBRA audits, which may signal an increase in COBRA compliance audits.

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At a Glance...

Common COBRA Errors

Failure to provide COBRA notices

Common errors include failing to provide any or all of the four required COBRA notices to all qualified beneficiaries, or providing notices late. These notices include the COBRA General Notice, the COBRA Election Notice, the Notice of Unavailability of Group Health Coverage, and the Early Termination Notice.

Failing to provide the COBRA Election Notice, or providing it late, is particularly complex because there may be coverage issues with the insurance carrier. In the worst case, the insurance carrier may refuse to cover the qualified beneficiary(ies), leaving the employer liable for the cost of medical care.

Failure to offer COBRA continuation coverage

An employer's failure to offer COBRA continuation coverage has ramifications. For this reason, employers should seek legal guidance as soon as possible after detecting an error.

Reduce Financial Exposure

Engage specialists

Due to the complexities of COBRA administration, the significant financial penalties for noncompliance, and the anticipation of increased oversight by COBRA auditors, employers are advised to engage specialists in COBRA administration. By taking a proactive approach to ensuring that COBRA regulations are followed in an appropriate and timely manner, employers should be well-positioned in case of an IRS audit.

COBRA Audits – Know Your Answers!

Possible questions during a COBRA audit

The following questions may be raised during a COBRA audit:

- How many qualifying events occurred during the audit year through the current date?
- How do you notify participants of their COBRA rights?
- How do you notify the plan administrator that a qualifying event has occurred?
- What COBRA elections were made by qualified beneficiaries?
- What amount of premiums have been paid by qualified beneficiaries for COBRA coverage?

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In March 2012, the IRS issued revised guidelines for COBRA auditors, raising concerns among many employers about documentation, noncompliance, and the risk of significant financial penalties.

Ever since its passage in 1986, the Consolidated Omnibus Budget Reconciliation Act ("COBRA") has posed significant challenges to employers and administrators of group health plans. This white paper will help you understand and navigate through these complex issues.¹

COBRA Coverage



Which employers must comply with COBRA?

In general, plans sponsored by private sector companies that employed a minimum of 20 full-time workers — or the equivalent* — on more than 50 percent of business days in the previous calendar year must comply with COBRA.

Ever since its passage in 1986, COBRA has posed significant challenges to employers and administrators of group health plans.

Standards and rules

COBRA continuation coverage generally must be identical to the coverage offered to similarly situated non-COBRA beneficiaries under the group's health plan. This coverage includes plan features and changes to plan features, such as:

- Benefits, choices, and services
- Copayments, deductibles, and coverage limits
- Rules for filing claims and appealing denied claims
- Right to change coverage options during open enrollment



Health plans subject to COBRA

COBRA regulations specify the types of group health plans that generally are subject to COBRA. These include:

- Medical and prescription drug plans
- Dental plans
- Flexible Spending Accounts (FSAs)
- Health Reimbursement Accounts (HRAs)
- Health Maintenance Organizations (HMOs)
- Vision plans
- Group health plans sponsored by state and local governments
- Certain Employee Assistance Programs (EAPs) — those supplying medical care

* According to guidelines issued by the Department of Labor, companies must calculate the number of full-time equivalent (FTE) workers they employed during the previous calendar year. This calculation includes full-time and part-time employees. Each part-time employee counts as a fraction of an employee, with the fraction equal to the number of hours that a part-time employee worked divided by the hours an employee must work to be considered full time.²

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Those exempt from COBRA include:

- Plans sponsored by the federal government (Medicare, Medicaid)
- Plans sponsored by certain religious organizations
- Health Savings Accounts (HSAs)

Qualified Beneficiaries



Qualified beneficiaries

Individuals who qualify for continuing coverage under COBRA are designated "qualified beneficiaries." To be considered a qualified beneficiary, an individual typically must have been covered by a group health plan subject to COBRA the day before the occurrence of a "qualifying event." (see Qualifying Events)

Qualified beneficiaries may include:

- Covered and former employees
- Spouses, former spouses, or spouses legally separated from covered employees
- Dependent children*, including adopted children or children legally placed for adoption
- Agents, independent contractors, and directors who participated in the group health plan

Additional qualified beneficiaries

The bankruptcy of an employer may create additional qualified beneficiaries, including: retired employees, their spouses, former, or legally-separated spouses, and their dependent children, or children placed for adoption or adopted by the former qualified beneficiaries. In the event of a bankruptcy, the company should consult with its own legal counsel to determine its obligations under COBRA.

Qualifying Events and Duration of Coverage



Qualifying events

An individual can become a qualified beneficiary only if a qualifying event has occurred. As depicted in the following chart, qualified beneficiaries and the length of eligibility for continuation coverage generally depend on the type of qualifying event.

* Under health care reform, health plans are required to extend coverage to children up to age 26. This mandate extends the age of dependent coverage under COBRA as well.³

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Termination (whether voluntary or involuntary) for reasons other than gross misconduct or reduction in hours of employment	Employee Spouse Dependent child	18 months
Employee entitlement to Medicare resulting in a loss of coverage	Spouse Dependent child	36 months
Divorce or legal separation	Spouse Dependent child	36 months
Death of employee	Spouse Dependent child	36 months
Loss of dependent child status under the plan	Dependent child	36 months

Note: Some eligibility restrictions may apply.

Factors extending length of COBRA continuation coverage

The maximum amount of coverage available is 36 months from the original qualifying event. Three factors can affect the length of COBRA continuation coverage: (1) the employee's entitlement to Medicare; (2) the disability of a qualified beneficiary; and (3) a second qualifying event. In addition, at the plan's discretion, coverage may be extended longer than the maximum length required by law. However, the insurance carrier must agree to such an extension.

Medicare entitlement

When the qualifying event is termination or reduction of the employee's hours, and the employee became entitled to Medicare less than 18 months before the qualifying event, then the employee's spouse and dependents are eligible to continue coverage for a maximum of 36 months after the employee's Medicare entitlement date.

Disability

If a qualified beneficiary becomes disabled and meets certain requirements, all qualified beneficiaries are entitled to an 11-month extensions of continuation coverage, up to a total maximum period of 29 months. (See Disabled Qualified Beneficiary).

Second qualifying event

Should a second qualifying event occur, qualified beneficiaries may receive an 18-month extension of continuation coverage, for a total of 36 months from the original qualifying event.

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Factors causing early termination of coverage

A group health plan may terminate COBRA continuation coverage earlier under certain conditions. These factors include:

- nonpayment or late payment of premiums;
- employer's cessation of any group health plan;
- qualified beneficiary's beginning coverage under a new group health plan, unless the new plan imposes pre-existing condition exclusions or limitations;
- qualified beneficiary's becoming entitled to Medicare;
- qualified beneficiary's engaging in fraud or other conduct justifying termination of coverage.

Notification Rules for Group Health Plans and Employers

COBRA requires group health plans to include specific information in their plan documents. COBRA rights must be detailed in a plan's Summary Plan Description (SPD), and material modification of COBRA rights must be described in a plan's Summary of Material Modifications (SMM).

Notification to plan participants of COBRA rights and changes

Group health plans are required to notify plan participants of their COBRA rights and material changes to their COBRA rights. These notifications must be provided within 90 days following the date on which plan coverage originally begins or material changes take place. The 90-day notification rule may be satisfied by providing participants with a plan's SPD and SMM within the 90-day period.

Notification responsibilities related to qualifying events



Employer responsibility

The employer is responsible for notifying the group health plan within 30 days when one of the following qualifying events occurs: termination or reduction in the hours of a covered employee's employment, a covered employee becoming entitled to Medicare, or the death of a covered employee.

Group health plan responsibility for COBRA election notices

A group health plan has 14 days following notice of a COBRA qualifying event from the employer to provide all qualified beneficiaries with election notices. In general, election notices outline the rights of qualified beneficiaries

COBRA rights must be detailed in a plan's Summary Plan Description (SPD), and material modification of COBRA rights must be described in a plan's Summary of Material Modifications (SMM).

Employers or plan administrators and employees or qualified beneficiaries have notification responsibilities related to qualifying events.

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to continuation coverage and describe how qualified beneficiaries may elect continuation coverage.

Group health plan notice of unavailability of COBRA continuation coverage

If a group health plan determines that an individual is not entitled to continuation or extension of coverage, the plan must notify the individual within 14 days after the notification of a qualifying event and state the reason for the determination.

Special COBRA notice rules for multi-employer plans

Multi-employer plans are permitted to adopt certain special rules regarding COBRA Notices. Special rules include: adoption of uniform time limits for qualifying event or election notices, elimination of the requirement that employers provide qualifying event notices, and instead have determination by the plan administrator of when a qualifying event occurred.

Notice of early termination of coverage by a group health plan

In the case of early termination of coverage, a group health plan must notify the qualified beneficiaries as soon as possible following the decision. The notice must include the date coverage will terminate, the reason for termination, and any rights the qualified beneficiary may have under the plan, or under an applicable law, to elect alternative group or individual coverage.

Qualified Beneficiary Responsibilities, Election Procedures, and Rights

Employee or qualified beneficiary responsibility

A qualified beneficiary is responsible for notifying the group health plan within 60 days when one of the following qualifying events occurs: divorce of a covered employee, legal separation of a covered employee and spouse, or loss of dependent status of a child of a covered employee.

Election periods



Group health plans must give qualified beneficiaries 60 days to decide whether or not to elect continuation coverage. The 60-day election period begins on the later of (1) the date on which the election notice is provided to qualified beneficiaries; or (2) the date on which qualified beneficiaries otherwise would lose coverage due to qualifying events.

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Right to elect or waive COBRA coverage

With certain exceptions, when more than one individual becomes a qualified beneficiary at the same time due to the same qualifying event, the group health plan must give each qualified beneficiary an independent right to elect continuation coverage.

However, the covered employee or the covered employee's spouse may elect continuation coverage on behalf of all other qualified beneficiaries for the same qualifying event. In addition, the parent or legal guardian of a qualified beneficiary who is a minor child may elect or waive continuation coverage on behalf of the child.

Every qualified beneficiary who waives continuation coverage during the election period may later revoke the waiver and elect continuation coverage before the end of the election period. If a waiver is revoked later, the plan is permitted to begin continuation coverage on the date the waiver has been revoked.

Disabled Qualified Beneficiary

Three requirements must be met for the family of a disabled qualified beneficiary to receive extended continuation of coverage: (1) the Social Security Administration (SSA) must determine that the qualified beneficiary is disabled; (2) the disability must occur within 60 days of COBRA continuation coverage; and (3) the disability must continue through the remaining 18-month period of COBRA coverage.

Notice of disability

The disabled qualified beneficiary or another person on his or her behalf must notify the group health plan. The timing of the notice may be set by the plan. However, it may not be shorter than 60 days from the latest of the date on which the SSA issues the disability determination, the date the qualifying event occurs, or the date the disabled qualified beneficiary receives the COBRA general notice.

Termination of disability extension

If the SSA determines that the qualified beneficiary is no longer disabled, the right to a disability extension may be terminated and the qualified beneficiary may be required to notify the plan. The plan must allow the qualified beneficiary a minimum of 30 days following the SSA determination to provide notice.

If a qualified beneficiary is disabled, all qualified beneficiaries in the family are entitled to 11-month extensions of COBRA continuation coverage, for a total maximum period of 29 months.

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Costs and Payments



Costs

Group health plans may require qualified beneficiaries to pay premiums for COBRA continuation coverage or offer the coverage at no cost. In general, premium costs must be fixed in advance of 12-month premium cycles, but premium costs may be increased if plan costs increase and, during the 11-month disability extension, disabled qualified beneficiaries may be charged up to 150 percent of the full cost of coverage.

The maximum premium for a qualified beneficiary cannot exceed 102 percent of the cost to the plan for similarly situated individuals who have not incurred a qualifying event (both the portions previously paid by employees and any portion paid by the employer, plus 2 percent for administrative costs).

Payments



COBRA election notices must include premium due dates and the consequences of nonpayment. Group health plans must provide at least 45 days after the election of COBRA continuation coverage for qualified beneficiaries to make the initial COBRA continuation payment. The 45-day period begins on the date the qualified beneficiary sends the election form via first-class mail. If a qualified beneficiary fails to make any payment within the 45-day period, the qualified beneficiary's right to continuation coverage may be terminated.

Group health plans may require qualified beneficiaries to pay premiums for COBRA continuation coverage or offer continuation coverage at no cost.



Qualified beneficiaries must be permitted 30-day grace periods to make subsequent payments. If payment of the full amount of the premium is not received by the end of the grace period, the group health plan may terminate coverage.

If coverage is terminated early due to nonpayment of premiums, the group health plan is required to send the qualified beneficiary a notice of early termination.

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COBRA Audits, Noncompliance and Penalties

The following information outlines the extent of an audit and the rules and documentation an employer must have in place to avoid penalties.

Highlights of new COBRA audit guidelines

Some of the highlights of new COBRA audit guidelines include:

- Details about the IRS's COBRA enforcement strategy and specific examples of compliance violations;
- A list of documents auditors may request during a COBRA audit;
- A list of interview questions auditors may ask to determine noncompliance.⁴

Tax sanction for noncompliance

The tax sanction for noncompliance is hefty. As set forth in Internal Revenue Code (IRC) §4980B, it is an excise tax of \$100 or more per day, per qualified beneficiary, for each day of the noncompliance period.⁵

Documents requested during COBRA audit

During an audit, the IRS auditor may request and review the following documents:

- A copy of the COBRA coverage procedures manual;
- Copies of standard COBRA coverage letters sent to qualified beneficiaries;
- A copy of the plan sponsor's internal audit procedures for COBRA coverage;
- Copies of all of the plan sponsor's group health plans;
- Details pertaining to any past or pending lawsuits filed against the plan sponsor alleging COBRA failures;
- Copies of federal and state employment tax returns;
- A list of all individuals affected by qualifying events during the audit year;
- Personnel records (including name and address of each qualified beneficiary, the qualifying event date, copies of COBRA notices, the type of COBRA coverage received, and the premium payments required under COBRA).⁶

While errors do sometimes occur in COBRA administration, there is little official regulatory guidance on correcting errors. To avoid noncompliance penalties, employers should seek legal counsel as soon as possible after detecting an error.

AHA COBRA Services...

COBRA Administration

AmeriHealth Administrators is a national third-party administrator with more than 20 years of COBRA administration experience. AHA's COBRA specialists help employers fulfill complex COBRA regulations, which can help employers avoid severe penalties for noncompliance. Specific services include:

- Updating required rules and information in plan documents;
- Providing notifications to plan participants of COBRA rights and changes;
- Providing notifications related to qualifying events;
- Maintaining records related to election, duration, termination, and unavailability of continuation coverage;
- Managing conversion options (if applicable);
- Managing costs and payments;
- Online services.

For additional information about AmeriHealth Administrators and their comprehensive COBRA administration services, please contact your Independence Blue Cross sales representative.

Appendix

COBRA Continuation Law Jurisdiction and Administration

The Departments of Labor and Treasury have jurisdiction over private sector group health plans. The Department of Health and Human Services administers the COBRA continuation law as it affects public sector group health plans.

Sources of information on COBRA

Information needs	Sources
Information regarding COBRA, ERISA, or HIPAA	<p>Employee Benefits Security Administration (EBSA)</p> <ul style="list-style-type: none">• Call 1-866-444-3272• Visit www.dol.gov/ebsa; click on Publications/Reports, then click on Compliance Assistance Guide - Health Benefits Coverage Under Federal Law
Information about COBRA	<p>Employee Benefits Security Administration (EBSA)</p> <ul style="list-style-type: none">• Visit web site www.dol.gov/ebsa/cobra.html
Information regarding COBRA and the Family and Medical Leave Act (FMLA)	<p>U.S. Department of Labor</p> <ul style="list-style-type: none">• Visit www.dol.gov/whd/fmla
Information regarding the Health Coverage Tax Credit (HCTC): Trade Adjustment Assistance Extension Act of 2011	<p>Internal Revenue Service (IRS)</p> <ul style="list-style-type: none">• Visit www.irs.gov/Individuals/HCTC:-Trade-Adjustment-Assistance-Extension-Act-of-2011
Information regarding Uniformed Services Employment and Reemployment Rights Act (USERRA)	<p>U.S. Department of Labor</p> <ul style="list-style-type: none">• Visit www.dol.gov/compliance/laws/comp-userra.htm

References

- 1 Unless otherwise noted, the guidelines in this white paper are provided by the Department of Labor (DOL) at www.dol.gov.
- 2 Internal Revenue Code (IRC) Section 4980B (www.irs.gov)
- 3 “Extending Child Coverage Up to Age 26—COBRA Implications,” Hamburger, Paul M., Society for Human Resource Management (SHRM), 6/2/2010.
- 4 “Audit Techniques and Tax Law to Examine COBRA Cases (Continuation of Employee Health Care Coverage),” www.irs.gov.
- 5 Audit Techniques and Tax Law to Examine COBRA Cases, *ibid.*
- 6 Audit Techniques and Tax Law to Examine COBRA Cases, *ibid.*



This white paper contains a summary of COBRA Continuation Coverage and is not intended to provide legal or tax advice. Please consult with your legal or tax advisor for specific legal and/or tax advice with respect to your obligations under COBRA.