

COBRA Final Regs Bring On Answers...And Many Questions

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There's a lot happening at the federal level these days, and when I considered writing on many issues, I was soon overwhelmed with one in particular, the new and proposed COBRA regulations, released this month. Therefore, I decided to narrow my focus to this one very important issue. In the next issue, I'll discuss some of the other happenings in Washington, D.C., along with our Capitol Conference report.

The IRS has issued its final regulations to the Consolidated Omnibus Reconciliation Act, COBRA. Unfortunately, they leave many unanswered questions, which will undoubtedly have attorneys, arguing and looking for interpretations for many months, or perhaps years, to come. In addition, new proposed regulations accompany the final regs.

Jim Trimble, Vice President, ABR Benefit Services, Inc., a leading national COBRA administrator, discussed the new and proposed regulations with me. "Nearly thirteen years after the enactment of COBRA in 1986, and the issuance of initial COBRA proposed regulations in 1987, the Internal Revenue Service has now issued what it refers to as its 'final COBRA regulations.' The final regulations contain clarifications of some past complexities, and introduce some new complexities that themselves will require further clarification."

Mr. Trimble discussed the purpose of the proposed regs. "The proposed regs address items that are not thoroughly dealt with in the final regulations." It is hoped that the proposed regulations, as well as their likely future dialogue, will answer some of the discrepancies that currently exist. The new regulations are effective upon the release date, February 3, 1999. As printed in the Federal Register, the final regs include the proposed regs, as well as a question and answer enclosure.

According to the Department of Treasury, (26 CFR Parts 54 and 602, RIN 1545-AI93), the "Proposed regulations interpreting the COBRA continuation coverage requirements were published in the Federal Register of June 15, 1987 and of January 7, 1998. This [the final regulations] document contains final regulations based on these two sets of proposed regulations. The final regulations also reflect statutory amendments to the COBRA continuation coverage requirements since COBRA was enacted... The regulations will generally affect sponsors of and participants in group health plans, and they provide plan sponsors and plan administrators with guidance necessary to comply with the law."¹

Further, in the Overview, the IRS document states its reason for the new regulations. "The regulations are intended to provide clear, administrable rules regarding COBRA continuation coverage. The regulations give comprehensive guidance on many questions under COBRA, with a view to enhancing the certainty and reliance available to all parties -- including employees, qualified beneficiaries, employers, employee organizations, and group health plans -- in determining their COBRA rights and obligations. The guidance is designed to further the protective purposes of COBRA without undue administrative burdens or costs on employers, employee organizations, or group health plans."²

For example, the regulations:

¹ Department of Treasury, Internal Revenue Service, 26 CFR Parts 54 and 602, RIN 1545-AI93, [4830-01-u]

² Department of Treasury, Internal Revenue Service, 26 CFR Parts 54 and 602, RIN 1545-AI93, [4830-01-u]

- Prevent group health plans from terminating COBRA continuation coverage on the basis of other coverage that a qualified beneficiary had prior to electing COBRA continuation coverage, in accordance with the Supreme Court's decision in *Geissal v. Moore Medical Corp.*
- Give employers and employee organizations significant flexibility in determining, for purposes of COBRA, the number of group health plans they maintain. This will reduce burdens on employers and employee organizations by permitting them to structure their group health plans in an efficient and cost-effective manner and to satisfy their COBRA obligations based upon that structure.
- Provide baseline rules for determining the COBRA liabilities of buyers and sellers of corporate stock and corporate assets and permit buyers and sellers to reallocate and carry out those liabilities by agreement. This will significantly enhance employers' ability to negotiate and to plan appropriately for the treatment of qualified beneficiaries in connection with mergers and acquisitions, while protecting the rights of qualified beneficiaries affected by the transactions.
- Limit the application of COBRA for most health flexible spending arrangements. This will ensure that COBRA continuation coverage under health flexible spending arrangements is available in appropriate cases without requiring continuation coverage where that would not serve the statutory purposes.
- Eliminate the requirement that group health plans offer qualified beneficiaries the option to elect only core (health) coverage under a group health plan that otherwise provides both core and noncore (vision and dental) coverage.
- Give employers, in determining whether the small-employer plan exception applies, the option of counting by pay period rather than by every business day, and provide, for that exception, for the consistent treatment of part-time employees through the use of full-time equivalents.”³

SUMMARY OF COBRA CHANGES

The final and proposed regulations make important changes in COBRA rules, forms and procedures. In summary, some of the provisions include:

- **Effective date.** The final regulations are effective for plan years beginning on or after January 1, 2000. However, it appears that plans may choose to follow the new final regulations before the year 2000. Plans must be operated in “good faith compliance” with a reasonable interpretation of COBRA. Compliance with the proposed regulations is deemed good faith compliance.
- **No “core coverage” election.** It appears that the neither final nor proposed regulations require COBRA beneficiaries to elect only core medical coverage in a plan that offers both medical and dental or other coverages. This is inconsistent with the 1987 rules. Plans may now require a beneficiary to choose or reject the *entire* benefits package.
- **Out-of-area coverage.** The final regulations require that COBRA beneficiaries who move out of a coverage area of an HMO must be offered coverage under any plan maintained by the employer that is available in the beneficiary’s new place of residence, even if the employer does not have employees in that area.
- **Other coverage.** Plans may not cut off coverage for beneficiaries who had other health plan coverage before electing COBRA. Coverage, however, may be cut off if the beneficiary becomes covered under another plan after making a COBRA election.
- **Third party payments.** A third party, including a hospital or an employer wishing to cover a new employee under the previous employer’s plan, may pay for a beneficiary’s COBRA coverage.
- **Provider inquiries.** Plan administrators are now required to respond to questions from hospitals and health care providers about the status of a beneficiary’s COBRA coverage and election rights.
- **Independent contractors.** If an independent contractor was covered by a group health plan during his or her engagement, he is eligible for COBRA coverage. Under the final regulations, however,

³ Department of Treasury, Internal Revenue Service, 26 CFR Parts 54 and 602, RIN 1545-AI93, [4830-01-u]

independent contractors are not counted in determining whether the employer has fewer than 20 employees and is eligible for “small employer” exclusions under COBRA.

- **Number of plans.** The new proposed regulations permit the employer to control the number of plans it maintains for COBRA purposes. A beneficiary has the right to make a COBRA election for each plan. Employers are allowed to combine its programs into one plan, thereby giving the COBRA beneficiaries one election, or provide a separate election for each type of coverage. Such decisions must be spelled out in the Plan Document and Summary Plan Description.
- **FSA’s.** The proposed regulations provide that *COBRA does not apply* to most flexible spending accounts, since the prior position (based on the 1987 regulations) of nontaxable reimbursements in exchange for reduction in taxable compensation resulted in no benefit from making after-tax COBRA contributions for medical reimbursement.
- **Part-time employees.** The proposed regulations provide that part-time employees are counted as “fractional” employees in determining whether or not an employer has fewer than 20 employees for purposes of the “small employer” exemption for COBRA.

AREAS THAT MAY SUBSTANTIALLY AFFECT THE EMPLOYER

When asked what may impact the employer substantially, given the release of the final and proposed regulations, Mr. Trimble was most concerned about the “*failure to pay*” rules set forth in the final regulations. “One of the significant areas in the final regs deals with the failure to pay a COBRA premium due in an ‘insignificant amount.’ They do not define ‘insignificant.’ Without a definition, you can’t say what it’s going to be. But they gave you, under the final regs, two directions to go; two mechanisms. One, the plan can treat the payment as satisfying the plan’s requirements when they are short, or (two) they can notify the qualified beneficiary of the amount of the deficiency, and grant him or her a ‘reasonable period of time,’ which they consider a safe harbor to be thirty days, for the deficiency to be paid. I see that as being a big, open question.”

With the previous COBRA changes that came out of HIPAA, one uncertainty was the wording on newborn children of “employees” (not spouses) being a new qualified beneficiary with its own election rights. Many thought the loose wording was simply an oversight; that the intent was for newborn children of employees and their spouses to be considered qualified beneficiaries. The final regulations appear to have clarified this. “The final regs still say the ‘covered employee’. It does not include the spouse,” according to Mr. Trimble, that is allowed to have a newborn child with qualified beneficiary rights.

But there are other areas of employer concern. “The proposed regs,” continued Mr. Trimble, “have opened some doors, such as what plan qualifies for the ‘small employer exemption.’ The old rule was fairly simple; that was that companies with a group health plan and 20 or more full or part time employees during 50% or more of the preceding calendar year were required to comply with COBRA. The new proposed rules consider each part-time employee as a ‘fraction’ of an employee. That becomes a long process, and to try to explain that is going to be extremely difficult.” The fraction calculation is a lengthy process. The number of hours that must be worked to be considered a “full-time” employee must be determined in a matter consistent with the employers “general employment practices,” although for this purpose not more than 8 hours per day and 40 hours per week may be used. An employer may count employees for each “typical business day” or may count employees for pay periods. “The formula is very complicated” according to Trimble.

STAY TUNED

I suggest you pay close attention over the coming months, as the “final” regs, in this instance, may not be final at all. You are encouraged to stay tuned... Further interpretations are coming daily. What you hear today may change tomorrow.

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on public data, and the author and Mr. Trimble were commenting and quoting on the rules as stated in the regulations. ABR Benefit Services, Inc. does not provide legal advice. Employers and readers should always consult their own in-house counsel on matters such as COBRA or other regulatory issues for opinions or conclusions.

Reference Sources: COBRA Continuation Coverage Requirements, Proposed Regulations 1999, Department of the Treasury, Internal Revenue Service, 26 CFR Part 54, RIN 1545-AW94; COBRA Continuation Coverage Requirements, Proposed Regulations 1999, Department of the Treasury, Internal Revenue Service, 26 CFR Parts 54 and 602, RIN 1545-AI93, Federal Register Excerpts.

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Originally published in The Statement, 1999, California Association of Health Underwriters. Reprinted in several publications in 1999 and 2000.