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Locke Lord QuickStudy: IRS Releases Guidance on COBRA Premium Subsidy

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On May 18, 2021, the Internal Revenue Service issued Notice 2021-31 ?(the "Notice") ?providing much anticipated guidance on implementing the COBRA subsidy provisions under the American Rescue Plan Act (the "Act"). As discussed in our prior post, the Act provides a 100% premium subsidy for individuals who are eligible for COBRA coverage as a result of an involuntary termination of employment or reduction in hours. The COBRA premium subsidy is available for a six-month period beginning April 1, 2021 through September 30, 2021. The Notice offers the guidance in the form of 86 FAQs, addressing issues ranging from who is eligible for the subsidy, what is an "involuntary" termination of employment and how to receive and report the payroll tax credit.

Below is a summary of the key points included in the Notice:

Eligibility for COBRA Premium Assistance

Assistance Eligible Individuals ("AEIs") include individuals (employees, spouses and eligible dependents) who (i) have lost group health plan coverage as a result of an involuntary termination of employment (other than for gross misconduct) or a reduction in hours (ii) are, or could have been, eligible for COBRA between April 1, 2021 and September 30, 2021 and (iii) elect COBRA coverage. The Notice clarifies several points:

- Eligibility for other coverage makes AEI ineligible for subsidy. An AEI will cease being eligible for the COBRA premium assistance if such individual is ***eligible*** for coverage under any other group health plan, such as through a new employer or a spouse's plan or is eligible for Medicare, regardless of whether such individual enrolls in such coverage. However, if the other group health plan imposes a waiting period, the individual's eligibility for COBRA premium assistance ends of the first day of the month immediately following the end of the waiting period, even though the individual declined the coverage.
- Medicare. An individual who is currently enrolled in Medicare and who loses group health coverage as a result of a reduction in hours or involuntary termination of employment is not eligible for the COBRA premium assistance, even though such individual may be eligible to elect COBRA coverage.
- Enrollment in individual health coverage. An AEI includes an individual who is currently enrolled in individual health coverage through a Health Insurance Exchange. However, such individual is not eligible for a premium tax credit to pay the cost of Exchange coverage during any month the individual is enrolled in COBRA coverage.
- Individual may become an AEI more than once. An individual can become an AEI more than once during the COBRA premium assistance period. An example in the FAQs clarifies that an individual who becomes an AEI on April 1, 2021 as a result of her involuntary termination of employment, then becomes ineligible for the subsidy by enrolling in a group health plan sponsored by the employer of the individual's spouse will be eligible

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for the subsidy if the individual's spouse has an involuntary termination of employment and loses group health plan coverage before September 30, 2021.

- Second qualifying event. If the original qualifying event was a reduction in hours or an involuntary termination of employment, and the individual remains covered by COBRA for an extended period due to a disability determination, second qualifying event, or an extension under State mini-COBRA, such individual could qualify for COBRA premium assistance to the extent the additional periods of coverage fall between April 1, 2021, and September 30, 2021.
- Retiree coverage. An individual who is offered retiree coverage that is provided under a group health plan that is separate from the plan under which COBRA continuation coverage is offered is not an AEI. However, if the retiree coverage is offered under the same group health plan as the COBRA coverage, such individual is eligible for COBRA premium assistance.

Self-Certification and Attestation

Although earlier released Department of Labor guidance included a form that individuals could complete attesting as to their eligibility for COBRA premium assistance, it was not clear whether an employer could require or rely on the form to obtain the payroll tax credit. The Notice confirms that an employer may, but is not obligated to, require individuals to self-certify or attest that they are eligible for COBRA premium assistance and not eligible for other disqualifying group health plan coverage or Medicare. The employer may rely on such attestations to claim the payroll tax credit and must keep either a record of an individual's self-certification/attestation or other documentation to substantiate that the individual was eligible for the COBRA premium assistance.

Reduction in Hours

The Notice confirms that any reduction in hours that results in a loss of coverage will cause a qualified beneficiary to be an AEI, regardless of whether the reduction in hours is voluntary or involuntary. This includes furloughs, leaves of absences or a lawful work stoppages, such as a strike, so long as the employer and employee intend to maintain the employment relationship.

Involuntary Termination of Employment

The Notice defines "involuntary termination" generally as "a severance from employment due to the independent exercise of the unilateral authority of the employer to terminate the employment, other than due to the employee's implicit or explicit request, where the employee was willing and able to continue performing services." The determination of whether a termination of employment is involuntary is based on the facts and circumstances. The Notice provides the following examples of terminations that may constitute involuntary terminations of employment:

- Termination while absent due to illness or disability. An employer's termination of employment due to absence from work due to illness or disability constitutes an involuntary termination of employment ***only if*** there was a reasonable expectation that the employee will return to work after the illness or disability has subsided.
- Voluntary termination for Good Reason. An employee's termination of employment for "good reason" may constitute an involuntary termination if the termination is due to an employer action that results in a material negative change in the employment relationship analogous to a constructive discharge. This may include terminations designated as voluntary or a resignation if the facts and circumstances indicate that the employee was willing and able to continue performing services for the employer.
- Participation in Window Program. An involuntary termination includes participation in a voluntary severance

program that constitutes a “window program” under which employees with impending terminations of employment are offered a severance window to terminate employment within a specified period of time.

- Non-renewal of employment contract. An employer’s decision not to renew an employee’s employment contract will be considered an involuntary termination of employment if the employee was otherwise willing and able to continue the employment and execute another contract. However, if the parties understood, at the time they entered into the contract, that the contract would not be renewed, the non-renewal would not be an involuntary termination of employment.

The following examples ***will not*** qualify as involuntary terminations of employment:

- Retirement. A retirement is a voluntary termination of employment unless, absent the retirement, the employer would have terminated the employee’s employment.
- Death of employee. The death of an employees is not a reduction in hours or an involuntary termination of employment.
- Terminations for personal reasons. An involuntary termination would not include an employee’s resignation due to a child being unable to attend school or daycare due to COVID-19 closures.

Calculating the COBRA Premium Assistance Credit

In general, if an employer does not subsidize COBRA premium costs for other similarly situated qualified beneficiaries who are not AEIs, the applicable credit that the employer may claim per calendar quarter is an amount equal to the COBRA premiums that were not paid by the AEIs for COBRA continuation coverage due to the application of the Act. For this purpose, the premium amount also includes any administrative costs otherwise allowed (that is, generally 102 percent of the applicable premium under COBRA).

If an employer subsidizes COBRA coverage for other similarly situated qualified beneficiaries, the amount of the credit is the premium that would have been charged to an AEI in the absence of the premium assistance, and does not include any amount of subsidy that the employer would have otherwise provided. In other words, the credit is equal to the amount that the employer actually would have charged to the AEI. For example, as part of a severance package an employer subsidizes coverage for involuntarily terminated employees for a period of three months. The premium assistance credit can be claimed only for the reduced premium that would have been paid by the terminated employee for those three months. However, if the employer increases the employee’s premium obligation from the previous, reduced amount, the employer can claim the increased tax credit.

If an employer does not subsidize COBRA directly, but provides a taxable lump sum payment to employees who are AEIs which is intended for COBRA, the employer can claim the full amount of the tax credit.

In its guidance, the IRS also addressed the following special situations relating to calculating the premium assistance credit:

- Adjusting for Premium Changes. The premium assistance credit will adjust for changes in the amount of COBRA premiums for similarly situated covered employees and qualified beneficiaries (up to the maximum premium allowed under COBRA).
- Electing Different Benefit Packages. The premium assistance credit will apply to an increased premium if the plan allows the AEI to change coverage from the benefit package that covered the individual had before the

qualifying event to a different benefit package with a higher applicable premium.

- Not Applicable to Non-Federal Coverage. If COBRA continuation coverage is provided under a State program that provides comparable continuation coverage, the premium assistance credit will not apply to the portion of the premium attributable to COBRA continuation coverage for individuals who would not be qualified beneficiaries under Federal COBRA.
- Allocating the Credit Among AEIs and Non-AEIs. If COBRA continuation coverage of one or more AEIs also covers one or more individuals who are not AEIs, for purposes of calculating the premium assistance credit, the premium for the continuation coverage is allocated first to the premiums for the AEIs, based on the cost of COBRA continuation coverage (without COBRA premium assistance) for only AEIs, and then to the premiums for the individuals who are not AEIs.

Example: An employee and her two dependent children are AEIs and have COBRA continuation coverage. COBRA continuation coverage also covers an individual who lives in the same household who is not an AEI. The amount the plan requires to be paid for COBRA continuation coverage for self-plus-two-or-more-dependents (which includes the individual who is not an AEI) is $1,000 per month. The amount the employee would pay (absent the COBRA premium assistance) for coverage for the employee and the two children (the AEIs) for COBRA continuation coverage is $1,000 per month. The additional premium amount for coverage of the individual who is not an AEI is effectively $0 per month. The employee is entitled to apply the COBRA premium assistance for the full $1,000 premium amount per month. Therefore, the credit is $1,000 per month.

Claiming the COBRA Premium Assistance Credit

The party with the right to claim the premium assistance credit under the Act is the “premium payee” with respect to the applicable continuation coverage. For this purpose, a “premium payee” will include: (a) the common law employer maintaining the plan, in the case of a group health plan that is subject to Federal COBRA and is, in whole or in part, self-funded; (b) an insurer providing the coverage, in the case of fully insured plan subject to State mini-COBRA requirements; or (c) a multiemployer plan, in the case of a group health plan that is a multiemployer plan (as defined in § 3(37) of ERISA). For this purpose, a “premium payee” can include a governmental employer.

Once the party that is eligible for the premium assistance credit has been identified, the timing and method for claiming the credit must be addressed.

According to the Notice, the premium payee is entitled to the premium assistance credit as of the date on which the premium payee receives the AEI’s election of COBRA continuation coverage.

The premium payee is immediately entitled to a credit for the premiums that were effectively not paid by the AEI for all periods of continuation coverage that pre-date the day on which he or she actually elected continuation coverage. The premium payee is also entitled to the credit in the future for the premiums that are not paid by the AEI as of the beginning of each period of coverage for which the AEI does not pay the premiums in accordance with his or her election.

Based on the timing described in the last paragraph, the credit is claimed by reporting the credit and the number of individuals receiving COBRA premium assistance on the designated lines of the premium payee’s federal employment tax return. In anticipation of receiving the credit to which it is entitled, the premium payee may:

- Reduce the deposits of federal employment taxes, including withheld taxes that it would otherwise be required to deposit, up to the amount of the anticipated credit; and
- Request an advance of the amount of the anticipated credit that exceeds the federal employment tax deposits available for reduction by filing Form 7200 (Advance Payment of Employer Credits Due to COVID-19).

Deposits may not be reduced, and advances may not be requested, for a credit for a period of coverage that has not begun. Deposits may only be reduced in anticipation of the credit to which the premium payee is entitled for a period of coverage as of the date the premium payee is entitled to the credit as described above. Similarly, the Form 7200 may be filed after the end of the payroll period in which the premium payee became entitled to the credit, and the form must be filed before the earlier of: (1) the day the employment tax return for the quarter in which the premium payee is entitled to the credit is filed, or (2) the last day of the month following that quarter.

The Notice clarifies that the premium payee must include any premium tax credit in its gross income for the taxable year, which includes the last day of any quarter with respect to which the credit is allowed.

Utilizing a Third-Party Payer

A premium payee is entitled to the credit even if a third-party service provider (e.g., payroll service provider or professional employer organization (PEO)) reports and pays the payee's federal employment taxes. Unless the third-party is treated as the premium payee because it maintains the group health plan under which continuation coverage is provided, the third-party provider is not entitled to the credit, even if it is considered an "employer" for other purposes.

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