

Benefits

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New COBRA Guidance Requires Employers To Overhaul Notices And COBRA Procedures

By Susan L. Letney and Sonia Macias Steele

Just over one year ago, the Department of Labor issued proposed COBRA regulations that contained dramatic changes to the content of COBRA notices as well as the manner in which notices were required to be issued. On May 26, 2004, the DOL finalized those regulations. The final regulations are substantially similar to the proposed regulations and will require prompt action by employers that sponsor health plans.

In addition, a recent interpretation by the Internal Revenue Service of the COBRA "second qualifying event" rules may cause immediate compliance problems for many employers. Given the amount of recent litigation surrounding COBRA coverage (and the potential penalties that could be assessed against an employer for failing to comply with COBRA's requirements), employers need to review their COBRA notices and procedures to ensure they comply with the latest regulatory guidance.

This Benefits Insight highlights the major changes of the COBRA regulations and the recent IRS ruling and offers a compliance plan for employers.

Effective Date

The final regulations apply to plan years beginning on or after November 26, 2004 (for calendar year plans, this is January 1, 2005). This deadline gives employers at least six months to incorporate the changes prescribed in the final regulations. For the period of time prior to the effective date, the DOL deems plans that comply with either the final regulations or the previously proposed regulations, including those plans using the model notices issued under each set of regulations, to be acting in good faith compliance with the regulations.

However, IRS Revenue Ruling 2004-22, discussed below, may require employers to take action prior to the effective date of the new COBRA regulations if their current practices are inconsistent with the ruling.

Notice Requirements

Initial or General Notice

The final regulations preserve the two most significant modifications of the proposed regulations. First, the final regulations require employers to provide an initial, or "general," COBRA notice to employees and their spouses within 90 days of the date the employee and/or qualified beneficiary becomes covered by the plan. An exception to this rule applies when an employee (or qualified beneficiary) becomes eligible for COBRA during that initial 90-day period. In such a case, the plan may choose to furnish only the COBRA election notice and omit the initial notice. Second, the regulations permit the initial notice to be supplied to the employee through the Summary Plan Description (SPD). However, if an employer chooses to serve notice through the SPD, such notice covers only the employee and not the spouse. As a result, employers who serve notice through the SPD still have to furnish a separate notice to a spouse.

"Reasonable Procedures" Required For Notices From Employees or Qualified Beneficiaries

The final regulations also maintain and clarify a plan's responsibility to establish "reasonable procedures" where an employee or a qualified beneficiary is required to notify the plan administrator of qualifying events, second qualifying events, or the beginning or end of a disability. These "reasonable procedures" should be spelled out in the plan's SPD and include (i) identification of the designated contact person to whom the notice should be given; (ii) the means by which notice should be provided; (iii) the time limits for giving notice (30 or 60 days, depending on the event); and (iv) the information the plan needs to provide continuation coverage. If the plan does not have "reasonable procedures" in place, then notice is considered provided if certain information is given *orally or in writing* to parties customarily considered in charge of the plan.

Notice of Disability From Employees or Qualified Beneficiaries

The final regulations also modify the timing triggers for disability notice from an employee or qualified beneficiary. Under the final regulations, an employee or qualified beneficiary must provide notice of a disability within 60 days of the latest of (1) the date of the Social Security Administration's disability determination, (2) the date of the qualifying event, (3) the date on which the qualified beneficiary would lose coverage under the plan, or (4) the date on which the qualified beneficiary is informed of his obligation to provide a disability notice (either through the plan's summary plan description or through the initial COBRA notice). These limits are only minimums; plans may create time periods or requirements that are more favorable to beneficiaries.

When Notice is "Furnished"

The preamble to the final regulations states that notice is generally deemed "furnished" on the date of mailing if sent by first-class, certified, or Express Mail, or on the date of transmission if transmitted electronically, with one exception: notice to the plan administrator from the employee or other qualified beneficiary of a qualifying event, for purposes of starting the 14-day time limit to provide an election notice, is not deemed to be sent to the plan administrator until the plan administrator has actually received it.

Model Notices

The final regulations include a sample initial notice as well as an "event" notice (a notice that must be given to an employee and/or a qualified beneficiary when a COBRA event has been triggered). The final regulations clarify that information which clearly specifies those plans to which the COBRA notice applies must be provided in the notice. In addition, the model initial notice no longer requires employers to identify both the plan administrator and the COBRA administrator, but instead requires only the name, address, and phone number of parties who can provide information about the plan and COBRA coverage. Also, both the initial and event model notices reflect Revenue Ruling 2004-22 (discussed below) and provide that a second qualifying event will extend the period of COBRA coverage only if that second event would have caused a covered spouse or dependent to lose coverage in the absence of the first event.

For all these reasons, employers who did not act on the proposed regulations should consider adopting the final model notices. Employers who already use the proposed model notices should update them according

to the final changes.

Unavailability Notice

In a new twist, if COBRA is unavailable or denied, employers must inform the employee or qualified beneficiary within 14 days of receiving notice of a qualifying event, second event, or disability determination. The employer must do so even if the notice from the employee or qualified beneficiary is *non-compliant* with the plan's "reasonable procedures." Although this type of notice is new, the DOL did not provide a model.

Termination Notice

According to the final regulations, if continuation coverage will terminate prior to the end of the maximum period of continuation coverage applicable to the qualifying event, the employer must notify the employee or qualified beneficiary "as soon as practicable" after the plan determines that coverage will terminate. Again, even though this is a new requirement, the DOL did not provide a model termination notice.

Medicare As a Second Qualifying Event Under COBRA: IRS Revenue Ruling 2004-22

Prior to the DOI's release of the final COBRA regulations, the IRS issued a ruling that caught many employers by surprise. In Revenue Ruling 2004-22, the IRS determined that entitlement to Medicare would not constitute a "second qualifying event" under COBRA (which would extend the COBRA coverage period of an affected former employee's spouse and dependents from 18 to 36 months) *unless* entitlement to Medicare would have, on its own, resulted in the employee's loss of health coverage. Under the Medicare Secondary Payer rules, an active employee's entitlement to Medicare (or the entitlement of such active employee's spouse) due to age cannot affect his or her right to health care coverage from the employer, and thus, on its own, can never be an initial qualifying event. However, if the employee is terminated during the 18 months following his or her entitlement to Medicare, then the termination of employment, coupled with the initial entitlement to Medicare, would extend the COBRA coverage period to 36 months for the employee's spouse and dependents.

This ruling does not alter the rule which has provided that if the entitlement to Medicare occurs within 18 months *before* the employee terminates employment (or has a reduction of hours), then COBRA will be extended to spouses and dependents for the longer of (i) 18 months from the termination of employment or reduction in hours or (ii) 36 months from the date of the Medicare entitlement. If, on the other hand, the entitlement to Medicare occurs *after*

the employee terminates employment, then the second qualifying event (Medicare) must be examined as if the first qualifying event (termination) had not occurred. As a practical matter, this means that the *timing* of the employee's entitlement to Medicare is critical to whether that employee's spouse and dependents are entitled to extended COBRA coverage.

For many employers, this ruling is at odds with both their current practice and the plain language of their COBRA notices. This is especially troublesome because some insurance companies, due to adverse selection concerns, are refusing to extend the COBRA period to 36 months when a former employee becomes entitled to Medicare *irrespective* of the wording of the employer's COBRA notice. Accordingly, if a court were to bind an employer by the plain wording of its COBRA notice, an insured employer could be forced to "self insure" those spouses and dependents for the extended COBRA period. To avoid the risk of "self-insurance," employers should immediately review and revise their COBRA notices if necessary.

What Employers Should Do

Although the final regulations become effective for most employers on January 1, 2005, employers should take the following steps immediately to ensure that their plans conform to the new regulations:

Revise COBRA notices to comply with the changes in the final regulations, or adopt the revised model initial and event notices;

- Create notices for COBRA unavailability and early termination;
- Consult with your insurance carrier and update plan documents and COBRA procedures, if necessary, to reflect that entitlement to Medicare is not a second qualifying event if it would not have caused a loss of coverage absent the first qualifying event;
- Update your Summary Plan Description (SPD) to include "reasonable procedures" for notice from qualified beneficiaries; and
- Update your SPD and other plan documents to include other administrative changes stipulated in the final regulations.

For further assistance, please consult one of our attorneys in the Employee Benefits Practice Group.