

February 17, 2009

Employee Benefits Alert

A Brave New World: The Stimulus Bill and Other Congressional Action Create New Obligations for Benefit Plan Sponsors

The President's signing of the American Recovery and Reinvestment Act of 2009 (the "Stimulus Bill") on February 17, 2009 is just one in a string of recent events which impose new obligations on sponsors of employee benefit plans. This client alert is intended to summarize the employee benefit developments raised by the Stimulus Bill, as well as some other issues now facing employers sponsoring health and retirement plans.

American Recovery and Reinvestment Act of 2009

Employers and benefit plan sponsors should note several items in the Stimulus Bill: the expansion of COBRA responsibilities; the change in withholding rates; the regulation of compensation paid to certain employees of companies which accept payments under the Troubled Assets Relief Program ("TARP"); an increase in the exclusion amounts available for certain qualified transportation fringe benefits; and changes to certain HIPAA obligations (discussed in a separate alert—please see michaelbest.com).

a. Expansion of COBRA Rights.

The Stimulus Bill expands COBRA coverage obligations for employers. Previously, employees had to pay up to 102% of the cost of coverage to continue coverage under the employer's group health plan following a qualifying event (e.g., reduction in hours, termination, divorce, etc.). The Stimulus Bill reduces the employee's payment obligation for coverage. Now employees who were involuntarily terminated from employment (other than for gross misconduct) between September 1, 2008 and December 31, 2009, may continue coverage under an employer's group health plan for up to 9 months by paying only 35% of the coverage cost. The U.S. government will subsidize the remaining 65%; however, it does so by reducing the employment tax obligation (withholding, FICA, etc.) for the employer (or for the plan or insurance carrier as the case may be). For example, suppose an employer sponsors a self-insured group

To comply with the new regulations, employers must:

- Comply with the new SCHIP special enrollment provisions (April 1, 2009). In addition, employers must amend their group health plan documents to incorporate this change and potentially issue a Summary of Material Modifications regarding same;
- Watch for and distribute notices to employees and the state regarding the availability of SCHIP programs and provide notice to the state regarding benefit plan offerings (once released by DOL and HHS);
- If desired, amend the defined contribution plan to avoid the 2009 required minimum distribution by the last day of first plan year on or after January 1, 2011 or 2012 (if governmental plan);
- Produce other necessary notices to comply with the new subsidized COBRA requirement (within 30 days of the date released by DOL) and consider amending group health plan to provide for same;
- Amend standard COBRA notices to account for subsidized benefit for future eligible participants;
- Watch for the release of the new withholding tables from the IRS to implement the new withholding amounts;
- Ensure that executive compensation practices are compliant with the requirements of the TARP program, if applicable.

Further, employers should:

- Evaluate the coverage offerings under the group health plan to ensure the plan is not discriminating against a condition which could be considered a major life activity, or make sure to have empirical evidence that the cost of such a benefit qualifies the plan for one of the EEOC's exclusions, or make sure to evaluate the risk and be comfortable with the exclusion.



health plan with a total premium cost for family coverage of \$1,000 per month. An eligible former employee could elect to continue coverage under the plan and keep such coverage for 9 months by paying \$350 per month. The employer would then claim the remaining \$650 per month as a credit against its employment tax liability. The same result appears to occur when the plan is a large insured plan. Where the plan is a small insured plan (i.e. not subject to federal COBRA), it appears the insurance carrier would claim the remaining amounts as a credit against its own withholding liability, not the employer. Where the plan is a multiemployer plan, the plan would claim the remaining amounts as a credit against its withholding liability, if any. Congress will reimburse employers, insurance carriers, or plans (as applicable) when the COBRA subsidy exceeds the employment tax liability.

The COBRA subsidy period ends upon the earliest of the following events to occur: (i) the expiration of the 9 months of subsidy payments; (ii) the date the participant's eligibility for COBRA would have ended based upon his or her termination date; or (iii) the date the participant becomes eligible for coverage under another group health plan. ***Although not entirely clear in the Stimulus Bill, it further appears that COBRA coverage can be terminated for the employee's failure to pay the 35% subsidy (as would ordinarily be the case). However, it also appears that the normal grace period for payment of COBRA premiums will also apply.***

The COBRA provisions of the Stimulus Bill are effective upon enactment. ***The Stimulus Bill is vague about when the subsidy becomes available—whether it becomes available no earlier than February 17 (enactment date) or March 1 (e.g., the typical date of the next full period of COBRA coverage under a plan).***

Additionally, the Stimulus Bill provides an election period for eligible employees who were terminated prior to the Stimulus Bill's enactment and who declined COBRA coverage at that time. Such employees may elect COBRA coverage within the 60 days following the date notice of the extended period for election (discussed below) is provided to the participant. This coverage is not retroactive to the employee's qualifying event. Rather the coverage begins on the first period of coverage beginning on or after the Stimulus Bill's enactment. ***Again, it is unclear whether this is February 17 or March 1.*** The COBRA coverage may continue for the remainder of the duration for which the COBRA coverage would have otherwise been available. Thus, an employee terminated on November 1, 2008 and who declined COBRA coverage at that time could elect COBRA coverage on March 1, 2009. Any claims incurred during the period from November 1, 2008 through February 28, 2009 would not be covered. Assuming premium payments are made and the employee does not become eligible for other employer-provided coverage, the employee would receive subsidized coverage through November 30, 2009. Further, assuming no intervening event occurs to extend COBRA coverage (e.g., disability), the employee could continue COBRA coverage from December 1, 2009 through May 31, 2010 (the remainder of the 18 months from November 1, 2008) provided the employee pays the entire COBRA premium.

The Stimulus Bill also allows employers to permit employees who elect COBRA coverage to elect a different coverage level than the level the employee had when the qualifying event occurred. However, this change is only permitted when the coverage elected does not have a premium greater than the prior coverage.

The Stimulus Bill provides some exclusions from this provision. The Stimulus Bill does not appear to extend to individuals who lost coverage due to divorce, losing dependent status, or even voluntary resignations (just COBRA qualifying events associated with involuntary terminations). Individuals who exhaust COBRA coverage prior to the expiration of the 9-month period do not receive an extension of coverage. The COBRA subsidy rights do not apply, or are reduced, for certain individuals with adjusted gross income in excess of \$125,000 for the taxable year (or \$250,000 for joint filers). The subsidy does not apply to COBRA rights in a flexible spending arrangement under a Section 125 plan. ***These exceptions may create many administrative difficulties. For example, it is not clear what constitutes an involuntary termination. Is acceptance of early retirement in lieu of termination an involuntary termination? Also, most COBRA administrators will not know the individual's adjusted gross income for the taxable year, particularly for joint filers, because they never receive this information. It is possible that this responsibility falls to the Internal Revenue Service to reconcile on the employee's next tax return. Further guidance is necessary.***

The Stimulus Bill requires changes to an employer's COBRA notice procedures. An employer must give notice that the subsidized benefit is available; that the participant may obtain coverage despite the participant having



previously declined coverage; and that the participant may enroll in different coverage, if permitted by the employer. Such notice must be issued to participants (including terminated employees) within 30 days of the date model notices are issued by the DOL. ***It appears the employer may amend its COBRA forms to comply with this requirement rather than wait for the DOL's model notice. The benefit to plan sponsors is that such earlier notice will shorten the election period for previously terminated employees.***

Additional changes apply to COBRA coverage which is partially subsidized by the Pension Benefit Guaranty Corporation and those individuals who have COBRA coverage which is subject to the Trade Act of 1974.

b. *Change to Payroll Withholding Rates.*

Currently, employers are required to withhold 7.65% of an employee's income to cover FICA (which consists of the Social Security tax and Medicare Tax). Certain limits apply based upon the amount an employee earns annually.

Under the Stimulus Bill, this amount will be reduced by the lesser of 6.2% or \$400 (\$800 for joint filers) for certain employees. The credit is purported to increase an individual's take-home pay to try to encourage spending.

The withholding rate change does not affect all employees. Nonresident aliens, individuals who are claimed as dependents by other taxpayers, and estates or trusts will not receive the credit. Additionally, the credit is reduced proportionally for individuals with an adjusted gross income over \$75,000 (\$150,000 for joint filers). Individuals making in excess of \$95,000 (\$190,000 for joint filers) will not receive a credit at all.

The IRS will issue new withholding tables which will provide the proper withholding amounts in 2009. This reduction is scheduled to expire after calendar year 2010.

c. *TARP Fund Recipients Must Meet Certain Executive Compensation Standards.*

The Stimulus Bill mandates that the Secretary of the Treasury issue standards which all TARP recipients must meet. The standards must address several issues, including:

- The existence of limits on incentive compensation that the top 5 highest paid executives of a company where the executives take unnecessary and excessive risks while the company has an outstanding TARP obligation;
- The recovery of any bonus, retention award or incentive compensation paid to any of the top 5 highest paid executives and the next 20 highest compensated employees when the company's financial disclosures are found to be materially inaccurate;
- Prohibition on golden parachute payments to the top 5 highest paid executives and the next 5 highest compensated employees while the company has an outstanding TARP obligation; and
- Prohibition on any payment or accrual of a bonus, retention award, or incentive compensation by certain groups of employees while a TARP obligation is outstanding. The employee group affected depends upon the amount of the TARP assistance accepted by the company. For example, only the highest paid executive is affected if the TARP assistance is less than \$25 million. If the assistance exceeds \$500 million, then the five highest paid executives and the next 20 highest paid employees are affected. Bonus payments required pursuant to written employment contracts executed before February 11, 2009, are unaffected by this provision; however, it appears that incentive compensation and retention awards are still subject to these limitations, regardless of their presence in a written employment agreement.

Other certification requirements also apply. If this provision affects your company or institution, legal counsel should be consulted.

d. *Transit Pass Benefits Level Increases.*

The Stimulus Bill permits employers to provide up to \$230 per month for qualified transportation fringe benefits to employees in the form of transit passes or van pooling. Previously the limit was \$120 per month. The new higher limit only extends through December 31, 2010.



Worker, Retiree, Employer Recovery Act of 2008 (“WRERA”)

WRERA provides temporary relief to certain defined benefit plan funding requirements which arose under the Pension Protection Act of 2006 (PPA). The funding standards were created to ensure that plan assets would be equal to the present value of plan liabilities. Defined benefit plans were provided a certain amount of time to meet certain threshold amounts which became progressively closer to 100%. WRERA extends the time by which a defined benefit plan must become fully funded.

Additionally, WRERA waives the required minimum distribution (RMD) mandate for defined contribution plans organized under current Internal Revenue Code Section 401(a), 403(a), 403(b), and 457(b) for 2009, but not beyond.

WRERA does not apply to the 2008 RMDs, including those that must be paid out on or before April 1, 2009. Also, RMD mandates were not waived for defined benefit plans. Additionally, WRERA does not change the fact that an individual’s required beginning date (generally age 70½ with some exceptions) will still be considered to have occurred in 2009.

Because the RMD rules do not apply to defined contribution plans in 2009, amounts otherwise paid out in 2009 from a defined contribution plan may be rolled over without being subject to the penalties ordinarily associated with such action, with some restrictions.

At this point, it is not clear whether these changes are optional or required. Employers seeking to choose the safe route will want to consider amending their plan to account for the change. If desired, plans must be amended to take advantage of the required minimum distribution relief. Amendments must be adopted by the last day of the first plan year beginning on or after January 1, 2011 (or January 1, 2012 for governmental plans).

In addition, WRERA made several technical corrections to the PPA, including clarification that distributions from a retirement plan could be rolled over to a surviving spouse’s IRA or a nonspouse beneficiary’s IRA on a tax free basis (previously non-spouse beneficiaries were taxed on such a distribution).

Children’s Health Insurance Program Reauthorization Act of 2009 (“SCHIP”)

The Children’s Health Insurance Program was designed to help subsidize state programs that provide health care coverage to uninsured children. SCHIP reauthorizes this program. It also makes changes to employer group health plans. Plans must provide to an eligible, but unenrolled, employee or dependent a special enrollment opportunity in the employer’s group health plan. The provision is similar to the special enrollment rights provided under HIPAA.

SCHIP provides that the employee has 60 days after the loss of coverage under a Medicaid Plan or state program, or after becoming eligible for assistance under a Medicaid plan or state program, within which to request coverage in the employer’s group health plan.

Employers who operate in states where a Medicaid or state program is available must provide notices to its employees in that state of the existence of such program(s). Further, the plan must disclose to the state, upon request, information about the benefits available under the group health plan. The disclosure must be sufficient to allow the state to determine whether it would be more cost-effective for the state to subsidize the employee’s cost of coverage under the employer’s group health plan (either to the employee or employer directly) or to provide supplemental benefits on its own.

SCHIP is effective April 1, 2009. Plans must comply with the law on that date. It is unclear whether group health plans must be amended by that date, or whether retroactive amendment will be possible.

Additionally, notices will need to be issued on or before the first plan year that begins after the date model notices are issued by the Departments of Labor and Health and Human Services. Congress has directed these agencies to issue the model notices no later than April 1, 2010.



Americans With Disabilities Amendment Act of 2008 (“ADAA”)

The Americans With Disabilities Act (“ADA”) affects employers administering group health plans because a group health plan is a term or condition of employment. Under the ADA, an employer may not discriminate against a qualified individual on the basis of his or her disability in the terms or conditions of that individual’s employment.

The ADAA amended the ADA’s definition of a “major life activity” to include several conditions which courts and the Equal Employment Opportunity Commission (“EEOC”) previously rejected through decisions and regulatory action. The ADAA adds activities such as reproductive activities, walking, eating, sleeping, standing, lifting and even concentrating. The ADAA also eliminates the mitigating measures standard which stated that if an individual could use a mitigating measure to control his or her disability, then he or she was not disabled. The ADAA appears to expand the conditions for which a group health plan must provide coverage. However, it is unclear whether this will actually be the case because the EEOC may not change its position that a cost-benefit analysis controls when evaluating whether a condition is excludable.

By way of background, when the ADA was passed, the EEOC issued both regulations and other interpretive guidance on the law. The regulations did not address the ADA’s effect on group health plans. Other interpretive guidance did. This other interpretive guidance also provided parameters through which an employer could perform a cost benefit analysis to determine if a condition which, even though disabling, had to be covered. Essentially, if the benefit to treat the condition was too expensive, and the employer could show this, the plan would not violate the ADA by excluding the condition.

Through the ADAA, Congress instructed the EEOC to issue revised regulations conforming to the broader interpretation of major life activity. It is unclear whether the EEOC, in conformance with this mandate, will restate the interpretive guidance applicable to group health plans or just revise its prior regulations.

The issue is significant as the ADA permits punitive damages against employers for violations with regard to this portion of the ADA. Although there are no clear answers yet, employers are encouraged to discuss this issue with legal counsel.

If you have any questions about the content of this Client Alert or any other questions regarding employee benefit plans, please contact Charles P. Stevens at 414.225.8268, or cpstevens@michaelbest.com; John L. Barlament at 414.225.2793, or jlbarlament@michaelbest.com; or Kirk A. Pelikan at 414.223.2529, or kapelikan@michaelbest.com.

This client alert is one of a series designed to provide summaries of the American Recovery and Reinvestment Act of 2009 (“The Act”) and information and guidance regarding opportunities and relief made available through The Act. All of The Act client alerts are available on Michael Best’s [Stimulus and Economic Recovery Team publications page](#). For additional information on this topic, please feel free to contact one of the authors of this alert or your Michael Best attorney.

If you are interested in learning about other provisions included in the Act, the Michael Best [Stimulus and Economic Recovery Team](#) is prepared to assist you in understanding the implications and in developing and implementing a strategy to secure the benefits of this unprecedented legislation. Specifically, we will assist you to identify opportunities, prepare appropriate proposals and make targeted contacts to secure funds. We will also work with you to ensure that your applications are tailored to meet your needs and that your funded projects proceed in compliance with award requirements and applicable laws.

