COBRA and the Affordable Care Act

The Consolidated Omnibus Budget Reconciliation Act (COBRA) requires employers to offer covered employees who lose their health benefits due to a qualifying event to continue group health benefits for a limited time at the employee's own cost. COBRA provisions are found in the Employee Retirement Income Security Act (ERISA), the Internal Revenue Code (Code), and the Public Health Service Act (PHSA). Employers with 20 or more employees and group health plans are subject to COBRA provisions. Most governmental plans, church plans, and certain plans of Indian tribal governments are exempt from COBRA. Employers should always consult with counsel about state continuation laws that are similar to COBRA and apply to small employers.

Qualifying Events

Only seven events can trigger COBRA obligations and offers of coverage. They are:

- Termination of employment
- Reduction of hours
- Divorce or legal separation
- Death of the covered employee
- A dependent child ceasing to be a dependent under the plan
- Entitlement to Medicare
- Bankruptcy

These events must lead to an individual's loss of coverage. For example, if a reduction of hours or entitlement to Medicare did not result in an employee's loss of benefit eligibility, there would be no obligation to offer COBRA coverage. Conversely, employees might experience a loss of coverage that does not trigger COBRA; for example if they fail to pay their portion of the premium or their employer stops offering coverage to spouses.

Affordable Care Act Impact on COBRA

The Patient Protection and Affordable Care Act (ACA) did not directly impact or change COBRA obligations for employers, but other changes in related regulations will determine how and when employers offer COBRA coverage to employees.

Beginning in 2015, to comply with the ACA large employers must offer their full-time employees health coverage, or pay one of two employer shared responsibility (play or pay) penalties. An employer is considered large, or an applicable large employer (ALE), if it has 50 or more full-time or full-time equivalent employees. Full-time employees are employees that average 30 hours a week or more. There are two methods that an ALE can use to determine which employees must be offered coverage to avoid penalties: the monthly method, and the measurement and look-back method. ALEs are also required to report on coverage that they did or did not provide.

Measurement and Look-Back Issues

Under the look-back method, the employer looks at how many hours the employee averaged during a look-back period called a "measurement period." Once the employer determines whether or not the employee worked full-time during the measurement period, that determination generally will apply throughout the related stability period regardless of how many hours the employee actually works (unless the employee's employment ends).

This means that if an employee was determined to be full time and benefits eligible at the end of a measurement period, outside of very narrow circumstances involving a bona fide change in position, if the employee's hours are reduced below 30 hours a week, the employee must remain benefit eligible for the remainder of the stability period. Prior to the ACA, most employers would remove an employee from the plan if the employee's hours were below the eligibility threshold and, if applicable, offer COBRA.

Although an offer of COBRA coverage constitutes an offer of coverage from an ACA perspective, it is unlikely that a COBRA offer will meet affordability requirements, which would expose the employer to potential penalties. This is because, although the employee's hours have dipped below the 30-hour threshold, the employee is considered full time through the end of the stability period.

Employers that are using the measurement and look-back method should take special care and review their eligibility policies in their plan documents and employee handbooks. An overly simple policy that merely sets eligibility for the group health plan at the 30-hour threshold and does not mention the ACA's measurement methods would create a conflict for the employer if an employee dropped below 30 hours during the stability period.

An employer would be forced to choose which regulations to break if its plan limited eligibility to employees working 30 hours or more, but the ACA related stability period required that the employer offer benefits to anyone who was deemed full-time at the end of the earlier measurement period, regardless of how many hours the employee worked during the stability period. Employers should consult with legal counsel to ensure their eligibility policy is ACA compliant.

Employers should also note that, if an employee's hours drop during the stability period, not only should the employee not be offered COBRA in lieu of the group plan, but also that the employee can only drop the benefit if the employer's cafeteria plan has adopted a newer "reduction in hours" change in status event. Under new rules, a plan may allow a participant whose hours are reduced below 30 hours a week as a result of a change in employment status to drop his or her employer-sponsored health coverage mid-year, regardless of whether the hour reduction caused a change in the employee's eligibility status. The IRS gave two conditions that must be met:

1. The employee has been in an employment status under which the employee was reasonably expected to average at least 30 hours of service per week and there is a change in that employee's status so that the employee will reasonably be expected to average less than 30 hours of service per week after the change, even if that reduction does not result in the employee ceasing to be eligible under the group health plan; and

2. The revocation of the election of coverage under the group health plan corresponds to the intended enrollment of the employee, and any related individuals who cease coverage due to the revocation, in another plan that provides minimum essential coverage with the new coverage effective no later than the first day of the second month following the month that includes the date the original coverage is revoked.

This would allow an employee, otherwise locked into coverage due to his or her employer's use of the ACA's measurement and stability period, to drop coverage during a stability period. Because this is a new optional event, employers that wish to provide the opportunity to employees should amend their plans.

Reporting Offers of COBRA Coverage

Under the ACA, individuals are required to have health insurance and ALEs are required to offer health benefits to their full-time employees. In order for the IRS to verify that (1) individuals have the required minimum essential coverage, (2) individuals who request premium tax credits are entitled to them, and (3) ALEs are meeting their shared responsibility (play or pay) obligations, employers with 50 or more full-time or full-time equivalent employees and insurers will be required to report on the health coverage they offer. Final instructions for both the 1094-B and 1095-B and the 1094-C and 1095-C were released in September 2015, as were the final forms for 1094-B, 1095-B, 1094-C, and 1095-C. Included in these instructions is information on reporting offers of COBRA coverage.

Employers should note that the guidance provided here follows the official final instructions provided by the IRS. As of December 2015, the final instructions conflicted with the FAQ provided by the IRS on the same subject. Employers that are unsure which rules to follow should consult with their counsel and be uniform in their decision. Employers that are part of a controlled group should consider selecting a uniform method of reporting offers of COBRA coverage across all members of the controlled group. Employers should always consult their tax professional or tax attorney for situation-specific guidance on which codes to use for a particular employee. The decision to use a particular code or codes might be influenced by factors not contained within example situations.

For a large fully insured health plan, if COBRA is offered to a former employee upon termination, it is not reported as an offer of coverage. On Line 14 of the 1095-C, employers should use code 1H (no offer of coverage) for any month in which the COBRA offer applies, and on Line 16 the employer should use codes 2A and 2B where appropriate. The former employee will receive a 1095-B from the carrier on the coverage they enroll in.

Example: An applicable large employer has fully insured coverage that costs $104.99 for the lowest cost employee-only coverage. COBRA is offered to an employee who terminates employment on February 10.

Part II Employee Offer and Coverage

	All 12 Months	Jan	Feb	Mar	Apr
14 Offer of Coverage (enter required code)		1E	1H	1H	1H
15 Employee Share of Lowest Cost Monthly Premium, for Self-Only Minimum Value Coverage	$	$ 104.99	$	$	$
16 Applicable Section 4980H Safe Harbor (enter code, if applicable)		2C	2B	2A	2A

A self-funded employer has two options for reporting coverage. If it is a large employer the employer can follow the fully insured instructions regarding the 1095-C, and also issue a 1095-B to an individual who enrolls in COBRA. As an alternative, the employer can report the applicable offers and coverage on the 1095-C for all months of the year (which would encompass months the individual was an employee and months that the individual was not full time or an employee). If a self-funded employer reports an offer of COBRA coverage to a terminated or part-time employee on the 1095-C, the employer would use code 1G on Line 14 for applicable months, and the appropriate 2 Series code on Line 16 for each month.

If an employee is offered COBRA due to loss of eligibility (for instance, due to a reduction in hours for an employer that uses the monthly method) the employee's coverage is reported in the same way and with the same code as an offer of coverage to any other active employee. This means that on Form 1095-C, Line 14, an employer would use the appropriate offer code, on Line 15 it would report the cost of COBRA coverage (minus the 2 percent administration fee) for employee-only coverage, and on Line 16 it would use the appropriate 2 Series code for each month, most likely indicating the employee enrolled in the coverage (2C) or that the employee is not a full time employee (2B). Employers are not required to meet the affordability requirements of the ACA for part-time employees.

Example: An applicable large employer that uses the monthly measurement method (not the measurement and look-back method) has fully insured coverage that costs $104.99 for the lowest cost employee-only coverage. The cost of COBRA minus the 2 percent administration fee is $343.10. COBRA is offered to an ongoing employee who did not average 30 hours a week or more in the month of January. The employee enrolls in the COBRA coverage. If the individual chose not to enroll, code 2B is the likely alternative to code 2C.

Part II Employee Offer and Coverage					
	All 12 Months	Jan	Feb	Mar	Apr
14 Offer of Coverage (enter required code)		1E	1E	1E	1E
15 Employee Share of Lowest Cost Monthly Premium, for Self-Only Minimum Value Coverage	$	$ 104.99	$ 343.10	$ 343.10	$ 343.10
16 Applicable Section 4980H Safe Harbor (enter code, if applicable)		2C	2C	2C	2C

If an employer offers coverage to a terminated employee or to an employee who loses eligibility on the group plan under a state's continuing coverage laws, that offer should be reported in the same manner as COBRA coverage.

COBRA and Health FSA Carryovers

In December 2015, the IRS released Notice 2015-87, which covered a variety of ACA related topics, and included further guidance on COBRA and health flexible spending account (health FSA) carryovers.

Carryover amounts for health FSAs should be included in determining the amount of the benefit that a qualified beneficiary is entitled to receive during the remainder of the plan year in which a qualifying event occurs.

Example: An employer maintains a calendar year health FSA that qualifies as an excepted benefit. Under the health FSA, during the open season an employee has elected to reduce salary by $2,500 for the year. In addition, the employee carries over $500 in unused benefits from the prior year. Thus, the maximum benefit that the employee can become entitled to receive under the health FSA for the entire year is $3,000. The employee experiences a qualifying event that is a termination of employment on May 31. As of that date, the employee had submitted $1,100 of reimbursable expenses under the health FSA.

Conclusion: The maximum benefit that the employee could become entitled to receive for the remainder of the year as a benefit under the health FSA is $1,900 (($2,500 plus $500) minus $1,100).

The maximum amount that a health FSA is permitted to require to be paid for COBRA continuation coverage (102 percent of the applicable premium) does not include unused amounts carried over from prior years.

Example: An employee elects salary reduction with respect to a health FSA of $2,000. The employer provides a matching contribution of $1,000. In addition, the employee carries over $500 in unused benefits from the prior year. The employee experiences a qualifying event that is a termination of employment on May 31.

Conclusion: The maximum amount the health FSA is permitted to require to be paid for COBRA continuation coverage for the remainder of the year is 102 percent of 1/12 of the applicable premium of $3,000 ($2,000 of employee salary reduction election plus $1,000 of employer contributions) times

the number of months remaining in the year after the qualifying event. The $500 of benefits carried over from the prior year is not included in the applicable premium.

A health FSA must allow carryovers by similarly situated COBRA beneficiaries if it allows carryovers of unused amounts for similar situated non-COBRA beneficiaries. Health FSAs can condition carryovers on participation in the next year's FSA and may limit the ability to carryover amounts to a maximum period.

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