

Update

May 12, 2006



COBRA Basics Series: Issue 1

Understanding COBRA's scope: Covered rights, plans, people

Summary

The Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) requires employer-sponsored group health plans to give participants the opportunity to temporarily continue their benefits in certain situations when coverage usually would be lost. While COBRA compliance means increased costs and administrative obligations for group health plans, the consequences of noncompliance are even greater: Employers that violate COBRA face stiff penalties under the tax code and ERISA, along with liability for any uncovered health expenses incurred by someone improperly denied COBRA coverage.

This *Update* is the first of a COBRA Basics series designed to help employers understand the COBRA rules. This initial article sketches COBRA's general scope; later issues will examine specific COBRA topics, including: notice requirements; election, payment, duration and termination of COBRA benefits; and special considerations in mergers and acquisitions.

What rights does COBRA provide?

COBRA gives employees – along with their spouses and dependents – a chance to continue coverage under an employer's group health plan in certain situations that normally would cause a loss of coverage. Not every situation leading to a loss of group health plan coverage triggers COBRA rights; participants must experience a "qualifying event" (discussed below) for COBRA to apply. In general, individuals experiencing a qualifying event must be given the opportunity to elect only the coverage they were receiving immediately before the qualifying event.

If elected, COBRA coverage usually lasts up to 18, 29 or 36 months, depending on the qualifying event and beneficiary involved (see page 2 sidebar for details). An employer may charge anyone electing COBRA the full cost of coverage, plus an administrative fee. Other than the

Maximum COBRA duration

Employee/spouse/dependent coverage lost due to employee's **termination or reduced work hours**:

- 18 months if no disability
- 29 months if qualified beneficiary is disabled within the first 60 days of COBRA coverage
- 36 months if spouse/dependent experiences a later qualifying event during initial 18 or 29 months of COBRA coverage

Spouse/dependent coverage lost due to **events other than employer's bankruptcy or employee's termination/reduced work hours**:

- 36 months

Retiree coverage lost due to **employer's bankruptcy**:

- For retiree: Lifetime of retiree
- For spouse/dependents: The earlier of the date of the spouse/dependent's death, or 36 months after the retiree's death

administrative fee and limits on length of coverage, COBRA beneficiaries generally have the same rights as other similarly situated individuals currently enrolled in the group health plan.

COBRA provides a floor, not a ceiling. Accordingly, employers are free to offer greater rights than COBRA guarantees and to charge less than the allowed amount. But employers should consult their carriers before extending any such rights.

What qualifies as a group health plan under COBRA?

COBRA covers any group health plan that provides health care to employees, certain retirees, and their families. Both fully insured and self-funded group health plans are subject to COBRA. These plans include:

- medical, dental and vision plans,
- prescription drug programs,
- health flexible spending arrangements (FSAs),
- health reimbursement arrangements (HRAs),
- employee assistance programs (unless services are limited to referrals),
- wellness programs (unless they simply promote general health or fitness) and
- treatment programs and clinics.

Exempt plans. COBRA exempts the following plans:

- small employer (those with fewer than 20 employees) plans,
- church plans and
- governmental plans (but continuation coverage might be available to many state and local government plan participants under the Public Health Service Act and to federal employees under the Federal Employee Health Benefits Program).

Qualified long-term care service plans, medical savings accounts (MSAs) and health savings accounts (HSAs) are also not generally subject to COBRA, although high-deductible health plans tied to account-based plans generally must comply. COBRA also does not cover income-replacement benefits, such as short- or long-term disability, accidental death and dismemberment, or life insurance plans.

Who has rights to continuation coverage under COBRA?

COBRA "qualified beneficiaries" include employees and their spouses and dependent children, if enrolled in an employer's group health plan on the day before they experience a COBRA qualifying event. Any child born to or placed for adoption with an employee during a period of COBRA coverage is also a qualified beneficiary. Finally, retirees and their family members who lose health plan coverage due to an employer's bankruptcy also have COBRA rights.

Each beneficiary has an independent right to elect COBRA coverage, so an employer must permit a switch from family to individual coverage if just one family member elects continuation benefits. Qualified beneficiaries

who get married, give birth or adopt a child while on COBRA also can add the new spouse or child to their coverage, although these added individuals don't necessarily become qualified beneficiaries. For example, if a former employee's daughter has elected COBRA coverage, she may enroll her newborn child in the plan, even though the child may not otherwise be eligible for coverage.

Exclusions. COBRA qualified beneficiaries do not include:

- **Domestic partners.** Domestic partners covered by an employer group health plan are not qualified beneficiaries under COBRA rules. An employer may choose but isn't required to extend some type of continuation coverage benefits to domestic partners. Any extensions voluntarily offered domestic partners should be confirmed in advance with carriers (e.g., stop-loss carriers).
- **Nonresident aliens.** Nonresident aliens receiving no U.S.-source income while enrolled in the group health plan generally do not have COBRA rights.

What qualifying events trigger COBRA rights?

Qualifying events that trigger COBRA rights vary, but the common denominator in all cases is that the event must cause loss of coverage under an employer's group health plan.

Employees. COBRA qualifying events for employees include:

- termination for reasons other than gross misconduct or
- reduction in work hours.

Changes from full-time to part-time status, leaves of absence, strikes, lock-outs, retirement and layoffs all trigger COBRA if group health coverage would be lost. Even if an employer fires someone for cause, the employee usually remains eligible for COBRA. The only exception is for termination due to "gross misconduct." The government has not defined gross misconduct, leaving employers to rely on court interpretations of the term, which can vary.

Spouses and dependents. For spouses and dependent children, COBRA qualifying events occur when the covered employee:

- experiences reduced work hours or termination for reasons other than gross misconduct,
- enrolls in Medicare,
- divorces or legally separates from the spouse or
- dies.

For an employee's child, losing dependent status under the plan also is a qualifying event.

Retirees. An employer's commencement of a bankruptcy proceeding is a qualifying event for retired employees and family members.

For additional information, please contact your Mercer consultant.

*This **Update** is for information only and does not constitute legal advice; consult with legal and tax advisers before applying this information to your situation.*

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