

## Final COBRA Regulations Raise New Issues for Businesses

**By Attorney Patricia F. Claire**

While a source of perpetual interest to benefits attorneys, the COBRA statute now is generating renewed interest among practitioners of business law. Final COBRA regulations governing the provision of continuation health care coverage to qualified employees and dependents recently have been issued by the Internal Revenue Service. This is the second set of final COBRA regulations issued within two years by the IRS, and these will affect many businesses. Some will be employers whose group health plans may not have provided COBRA coverage previously, others will be employers whose plans may no longer have this responsibility. In addition, there are now final rules that attempt to provide enlightenment on how to deal with COBRA coverage liability in the sale or purchase of a business. Business law practitioners should be familiar with these new rules which potentially affect many clients.

### **What is COBRA coverage?**

The Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) requires that for employers with twenty or more employees, persons covered by a group health plan of the employer on the day before a “Qualifying Event” can choose to continue their group health coverage, generally paid for by the individual rather than by the employer. Small group health plans are an exception to the COBRA requirements. Qualifying Events include employment-related events like termination or reduction in hours, and certain other events such as divorce or loss of dependent status under the health plan - as long as the event would cause the regular active employee group health coverage to be lost. The coverage is available for a limited period of time, ranging from eighteen to thirty-six months depending on the type of Qualifying Event.

The burden is on the employer to determine whether its group health plan is covered by COBRA. If so, it is the responsibility of the employer to see to it that the whole COBRA compliance management apparatus is in place, so that employees and dependents are properly notified of their rights, notices are provided in a timely manner to all “Qualified Beneficiaries” so they can elect to continue their group health care, coverage is made available on the required terms for the proper length of time, and other requirements are met. There is stiff liability for non-compliance, including daily penalties per Qualified Beneficiary whose rights are violated.

## **When must a company's health plan offer COBRA continuation group health coverage to employees?**

Because the COBRA statute took effect fifteen years ago, it may be many years since a company has examined the issue of whether or not it is required to offer COBRA continuation coverage. Because of the revised Federal rules, there now is a different formula for employers to use in determining if their group health plan must offer COBRA coverage, Reg. Sec. 54.4980B-2.

As noted, there are stiff penalties for failure to comply with the COBRA regulations. It is important for employers near the twenty employee count to decide each year if their plan comes under the COBRA rules. Not only are new, growing businesses affected, but also established companies, whether they are growing or down-sizing.

Employers with part-time employees, an increasing number of employers these days, will be especially affected by the new rules. However, other employers also may be affected. Here is what the regulations provide as the revised way to perform the nose-count (note: the count continues to be based on the preceding calendar year).

First of all, the definition of the persons who have to be counted is changed. Only common law employees will have to be counted. Self-employed persons, corporate directors, and independent contractors covered by an employer's group health plan no longer will have to be counted in determining whether the employer's plan must offer COBRA coverage. (These individuals still might qualify for COBRA coverage, however.)

Second, while part-time employees still will have to be counted, they only will have to count for a fraction of a full-time employee. Each full-time worker counts as one employee. The part-time hours worked are treated as a fraction of the hours required to be full-time. Note: the rules do not permit more than eight hours a day/forty hours a week to be the regularly required full-time schedule.

Example: If all employees are half-time, and the employer has twenty such employees, previously that employer's plan would have been required to offer COBRA coverage. Now the part-timers would total only ten employees, and that plan would not have to offer COBRA coverage. However, the COBRA requirements will still apply to any Qualifying Events occurring while the plan had been subject to COBRA.

Finally, the employer is considered to have normally employed fewer than twenty employees during a calendar year if it has fewer than twenty employees on at least fifty percent (50%) of its typical business days during that year. The employer may select from two different methods of performing this calculation. Whichever method is chosen must be used consistently for all employees and for the entire year.

**Be prepared for unexpected liabilities in the purchase and sale of businesses because of the COBRA rules.**

In the sale of a business, which company is responsible for the COBRA coverage of employees of the business being sold? In the past, COBRA regulations had provided little guidance on this issue. The final rules in Reg. Sec. 54.4980B-9 make an attempt to answer this question - whether the transaction is a stock sale or a sale or other transfer of substantial assets.

The intention of the final rule is to make certain that COBRA coverage is offered by one of the parties to the sale. The regulation makes it clear that the buyer and seller are free to allocate by contract the responsibility for offering COBRA continuation coverage. If COBRA coverage is provided by one party as the parties have agreed, then the other party has no COBRA obligations.

If there is a default, then the regulation establishes which party becomes liable for offering COBRA coverage: regardless of whether it is a stock sale or an asset sale or other transfer, the seller is responsible for COBRA coverage for what are called the "M&A Qualified Beneficiaries", basically the seller's covered employees and dependents.

However, in any stock sale and in a sale or other transfer of substantial assets in which the buyer essentially continues the business, if the seller ceases to provide a group health plan to any employee in connection with the sale, the buyer is considered to be a successor employer and becomes responsible for providing for COBRA coverage of any M&A Qualified Beneficiaries. This can result in individuals who have never had an employment relationship with the buyer, having to be offered COBRA coverage under the buyer's group health plan. The health insurance carrier should be consulted to determine how best to effect COBRA continuation coverage in such a case.

**Many other issues covered by the final COBRA regulations.**

The many other issues covered by the final COBRA regulations, including the treatment of health flexible spending arrangements as subject to COBRA, the interaction of the Family and Medical Leave Act and COBRA, and maximum coverage period rules, are beyond the scope of this article. However, each of these may raise issues for any employer with a group health plan subject to COBRA. These regulations attempt to settle issues that have been outstanding for years and yet created the prospect of liability for employers with non-complying health plans.

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