

15 Things the IRS May Ask Employers in a COBRA Coverage Audit

The IRS seems to be stepping up its efforts to ensure that employers comply with COBRA continuation coverage rules -- most recently by updating its standards for COBRA audits, which may require employers to provide at least 15 pieces of information to prove they complied with the law.

The COBRA statute has long provided for excise tax sanctions that the IRS can assess against noncomplying employers, plans, insurers and third-party administrators. However, such sanctions were rarely, if ever, imposed, primarily because no enforcement structure was in place to do so. But in 2010, the IRS indicated that entities failing to comply with COBRA are to self-report excise tax sanctions on Form 8928, Return of Certain Excise Taxes Under Chapter 43 of the Internal Revenue Code.

Then on March 26, the IRS posted on its website "[Audit Techniques and Tax Law to Examine COBRA Cases \(Continuation of Employee Health Care Coverage\)](#)," which summarizes the COBRA law and the penalties for noncompliance -- and, most key, explains the steps an IRS examiner will take in determining if a "taxpayer" failed to comply with COBRA. Here, the examiner can request up to 15 pieces of information (the first five items are required):

1. A copy of the COBRA coverage procedures manual
2. Copies of standard COBRA coverage form letters sent to qualified beneficiaries
3. A copy of the entity's internal audit procedures for COBRA coverage
4. Copies of all group health plans (If necessary, the examiner is to reconcile the books to the amount of health care expense deduction claimed on the entity's tax return to confirm that all plans are listed)
5. Details on any past or pending lawsuits filed against the entity for failing to provide appropriate COBRA coverage
6. The number of qualifying events (for example, terminations, reduced hours, etc.) occurring in the year under examination through the current date
7. How qualified beneficiaries are notified of their COBRA rights
8. How the plan administrator is notified that a qualifying event has occurred
9. The election made by qualified beneficiaries to continue health coverage
10. The premium paid by qualified beneficiaries for COBRA coverage
11. Copies of federal and state employment tax returns filed during the current period under examination and the preceding year
12. A list of all individuals affected by a qualifying event (for example, termination, death, etc.) during the current year
13. A list of all individuals covered on the current and preceding years for each plan (this list is to include all qualified beneficiaries)
14. Personnel records, which include documents to support the following items:
 - name and address of each beneficiary
 - the qualifying event date
 - copies of COBRA notices
 - the type of COBRA coverage received
 - premium payments required under COBRA
 - a copy of the employer's letter to the insurance company/plan administrator notifying them of a qualifying event
 - the reasons for the termination of COBRA coverage properly elected by a beneficiary
 - the reasons for employment termination
15. If the employer is denying coverage due to an employee's gross misconduct, the examiner can check to see if that employee was denied unemployment benefits for the same reason.

In addition, the examiner can make "third party contacts" with qualified beneficiaries to further validate certain information.

Excise tax sanctions can add up for noncomplying entities. Although mitigating factors can decrease -- or even eliminate-- the tax, generally, the maximum tax can be: (1) for single employer plans, 10 percent of the amount paid or incurred by the employer during the preceding tax year for group health plans, or \$500,000; and (2) for third parties such as insurers, \$2 million.

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