

September 30, 2008



A Member of M Financial Group

Ms. Amy O'Toole, Finance Officer
Town of Canton
4 Market Street, Suite 100
P.O. Box 168
Collinsville, CT 06022

**Re: Employment Agreements and Severance Packages
Commitments to Individuals Regarding Insurance**

Dear Amy:

We periodically are asked about the ability to extend or expand benefit and/or insurance coverage to specific individuals through Employment or Severance Agreements. The most common issues involve:

- (1) Waiving the waiting period for new hires when Group plans include an eligibility requirement,
- (2) Extending eligibility into Retirement where the Group plans do not provide for post-retirement eligibility,
- (3) Modifying or expanding the coverage level beyond the Group plan maximums,
- (4) Extending eligibility coverage for participants separating from service; and
- (5) Seeking to modify or by-pass Evidence of Insurability requirements for additional coverage.

Several important issues are raised when the Plan Sponsor commits to benefit or coverage statements that are not part of the existing Group Insurance Policy or Group Summary Plan Description. It is important to remember that the group health plan has an obligation to the insurance carrier to maintain the plan in accordance with the contract of insurance, (or, if self-insured, with the plan documents). The Plan Sponsor also has an obligation to the employees and their dependents, to administer the plan in their interests. These obligations are sometimes made more complicated when a workforce is covered under a collective bargaining agreement.

All too often, employers find that the promises they make with respect to early enrollment, continuation of benefits in separation agreements, or special arrangements with the soon-to-be-retired, conflict with the insurance contract, plan documents or summary plan descriptions. If the carrier does not accept or approve the request, there may be financial obligations requiring the Employer to "self-insure" the promise.

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At the very least, any such promises or statements should be qualified with some form of caveat such as "availability from the insurance carrier" and/or "subject to appropriate federal/state law." Otherwise, Plan Sponsors may find they have created, and taken on, a financial obligation for themselves with no offsetting insurance protection.

We recommend that prior to making any commitment regarding modifying eligibility, changing plan provisions, or extending coverage that you confirm with the appropriate carrier(s) that the proposed commitment can be incorporated into your group plan. You should also determine what, if any, impact there will be on your rate structure and who will bear the cost.

As always, we are available and willing to support you in any such discussions. We can also negotiate with the carrier(s), on your behalf, if policy changes are necessary. We can also assist in evaluating other options for delivering on your commitments.

We also strongly encourage involving your legal counsel if you are considering "customized" agreements. It is always best to include them before making any commitments or authorizing any exceptions.

The attached working outline provides some additional information on the most common types of requests. It does not represent legal advice and should not be construed as such. We welcome your questions and also encourage use of our HR Helpline at (860) 349-7010.

Sincerely,



Paul W. Lewis
Account Executive

PWL:mad
Enclosure

Employment Agreements and Severance Packages Commitments to Individuals Regarding Insurance

1. SITUATION:

Current plan eligibility requires waiting period, say “first of month following date of hire”. However, a prospective new hire asks for immediate coverage effective on date of hire.

Considerations:

- Your insurance carrier is under no obligation to provide eligibility and coverage other than as stated in your Summary Plan Description (SPD). You may request an exception (must be in advance of expected effective date) but must be sensitive to the non-discrimination requirements of plan administration.
- Such exceptions may create a precedent applicable to future such requests that you might not wish to accommodate.

Alternatives:

- (1) If the participant has COBRA continuation rights under their prior plan, you may offer to cover the interim premium for the prior plan’s coverage until the participant meets your Plan’s eligibility requirement.
- (2) Establish the date of hire to minimize the impact of the waiting period, if possible.
- (3) If the situation arises with sufficient frequency, consider changing your Plan’s eligibility rules for this class of participants. Be aware of non-discrimination requirements relative to Highly Compensated Employees (HCEs).

2. SITUATION:

Current plan eligibility terminates at Retirement but a request is made for extension of Life Insurance and/or Health Benefits (beyond COBRA or CT Continuation requirements).

Considerations:

- Life Insurance: insurance carrier is under no obligation to honor a commitment or pay a benefit not specified in the Policy. If you make a commitment for a Life Benefit without carrier approval, you will be obligated to pay the amount due.

Payments from an Employer are subject to Income Tax whereas insurance proceeds are not. There may also be non-discrimination issues.

- Health Insurance: insurance carrier is under no obligation to honor a commitment or pay a benefit not specified in the Policy. If you make a commitment for a Health Benefit without carrier approval, you will be obligated to pay the amount due for services received.

Employment Agreements and Severance Packages Commitments to Individuals Regarding Insurance

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Alternatives:

- (1) If the need for additional coverage is due to a regular increase in earnings and a multiple of earnings schedule, it is appropriate to ask the carrier to adjust its underwriting guidelines to allow a higher plan maximum; this should receive approval prior to any commitment to the participant(s).
 - (2) If the need for additional coverage is for a set dollar amount above and separate from the earnings schedule (e.g. 3 times Annual Earnings plus \$200,000), you should consider an Individual Term insurance contract. This is especially so when the commitment is for a pre-determined period of time or continues post-retirement. Such commitment should always be made contingent to "availability of an appropriate insurance policy".
 - (3) If the need is to continue some portion of the benefit into retirement (e.g. 3 times Annual Earnings while Active, reduced to a flat \$200,000 for x years of retirement), we again suggest one Individual Term policy. This isolates the liability, does not affect your accounting exposure and clearly defines the cost of the commitment. Again, such commitment should always be made contingent to "availability of an appropriate insurance policy".
4. **SITUATION:**
As part of an Employment or Severance Agreement, you wish to extend the time period a participant may continue in a benefit program beyond Statutory Guidelines. A common example: ABC Company will pay for X months of additional coverage and then place Participant on COBRA.

Considerations:

- Qualifying Event for COBRA is the date the Participant loses eligibility (e.g. no longer actively employed), not the date the Plan Sponsor stops paying for coverage.
- Insurance Carrier is only obligated for number of months specified by Statutory guidelines; any additional months become obligation of Plan Sponsor, with attendant exposure and income tax issues, without prior approval.
- Requests for non-standard Continuation durations pose non-discrimination concerns and may establish precedent relative to future requests (there are no secrets).

Alternatives:

- (1) You may offer to pay/contribute a set amount towards the cost of the benefit for any period beyond statutory guidelines. **This approach does not change your Policy, does not require exceptions, and does limit your cost exposure.**

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- Always consider your history of “past practices,” of granting or requesting exceptions, and the impact on future flexibility (precedent).
- Never make any commitment unless you are sure, in advance, you have an insurance offset (other than for an offer to pay premiums).
- Assess whether you are dealing with a “one off” or if there is sufficient volume to suggest a change to the Group Policy guidelines.
- Remember the Income Statement and Balance Sheet implications of extending benefits post-retirement; individual contracts may be a better answer.
- We are here to help; please let us know if you are considering extra-contractual commitments.
- Always consult your labor/employment attorney before finalizing the commitment, if in doubt, check twice!

These examples do not constitute legal advice and should not be construed as the basis for any legal documentation. Always consult with your legal counsel in preparing agreements and other such documents.