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Employee benefit minefields: Ensuring against false expectations

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Around this time of year, many companies start to take a hard look at their budgets, policies and practices. This is especially true this year, a time many perceive as a "soft" economy. With payroll and employee benefits as one of the largest expense items a company incurs, it is often these areas that employers will look at in order to meet austerity goals.

But as companies begin to consider what benefits they may want to change, or which employees they may no longer be able to keep, it is also a good idea to review some common mistakes regarding how certain insurance and other benefits have been presented -- or misrepresented -- to both incoming and outgoing employees.

Offer letters

Frequently, offer letters set forth a detailed combination of compensation and benefits to which the employee will be entitled if he or she accepts the offer. Often insurance benefits are a major factor in an employee's decision whether to take the job, especially when there are other dependants who will also be covered. On the other hand, insurance benefits are commonly modified -- and sometimes even eliminated -- depending on the very fluid (and still rising) health care costs.


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With this in mind, it is critically important to ensure that both the employer and employee understand that a company's health insurance coverage can be modified at any time. Otherwise, even an "at-will" employee can claim that the terms and conditions of employment were misrepresented in order to entice him or her to leave a prior employer. If the employee has moved from outside the county, a successful misrepresentation claim could also create a doubling of the employee's damages under Labor Code Section 972.

Several lawsuits arise each year from an inconsistency between the benefits set forth in the offer letter and the conditions attached to those benefits as set forth in a company handbook or plan benefit requirement. For example, an offer letter may state that an employee will be given two weeks vacation each year. But the offer may not explain whether the two weeks vests immediately or over time, whether the employee may actually take vacation within the first year, and it may even conflict with the actual company policy of providing Paid Time Off (PTO) in lieu of vacation.

The best way to guard against such problems is to avoid providing too much detail in an offer letter regarding the specific benefits currently in existence. Rather, the offer letter should simply make general reference to the company's handbook or other policy guide, which typically contains more explicit caveats with respect to the applicable rules of a given benefit, including the ability to change the benefit plan.

Auto insurance

If a company requires employees to drive as part of their job functions, chances are it already has a policy that requires those employees to have a valid driver's license and proof of current auto insurance. But the representation that an employee can drive on behalf of the company with "proof of

insurance" may give both the employer and employee a false sense of security in expecting coverage if an accident occurs.

In fact, most automobile insurance policies exclude coverage when a personal automobile is used for business purposes. Not only will the employee lack coverage for his own personal or property losses as a result of the accident, any third party injured in the accident will not be able to look to the employee's policy for recovery. In both cases, the employer will end up "holding the bag" and will be directly liable for any losses caused by the accident. Ironically, this may include losses suffered by the employee even for his own negligence. Labor Code Section 2802 generally requires an employer to reimburse an employee for any losses he or she incurs as a result of employment, except for the employee's gross negligence or willful misconduct.

Some employers try to guard against this problem by providing an automobile allowance to their employees and take the position that this allowance is intended to reimburse the employee for, among other things, any excess insurance costs associated with employees driving their own vehicles for business purposes. But even assuming the employees actually used the allowance for this purpose (unlikely), that coverage is only as good as its maximum limits and assumes the employee will remain current on his or her premiums. To properly guard against this risk, the employer should obtain its own auto and liability coverage for the business use of employee-owned vehicles.

Severance benefits

Some companies have a standard severance plan should an employee be terminated under certain conditions (i.e., a reduction in force or otherwise "without cause"). Others may provide severance on a more ad hoc, case-by case-basis. But in either case, where severance is provided to a terminated employee, the severance package often includes both a continuation of wages and a continuation of health insurance for a specified period.

Overlooked by many employers and employees alike is that several insurance companies will not allow an employee to remain on a group coverage plan if the employee is no longer working on a full-time basis.

Some carriers will not even cover employees if they are on nonmedical-related leaves of absence for extended periods of time. The problem typically arises where a terminated employee, whom the company still carries "on the books" as an employee for the purposes of group health insurance, subsequently develops a serious medical condition. The carrier will try to deny coverage and may find solid grounds to do so upon learning that the individual is no longer employed. In that circumstance, the employee will then look to the former employer -- who, after all, promised to provide continued insurance benefits as part of the severance package -- for compensation of all subsequent health care costs.

To avoid this problem, any severance agreement should specify the company's agreement to pay for a specified period of COBRA insurance coverage the employee may elect to obtain after separation from employment. This both prevents a potential coverage dispute later on and motivates the former employee to start looking for new employment sooner rather than later, as COBRA benefits are usually available for a maximum of 18 months.

Employers should therefore proceed with caution before making any type of promises, representations or modifications concerning the benefits they provide. This is especially true as the benefits packages companies offer continue to become of increasing importance to their most valuable -- albeit most expensive -- asset.

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