

COBRA SUBSIDY

The American Recovery and Reinvestment Act of 2009 (“ARRA”) provides for various forms of relief for low and moderate-income wage earners and their families and in particular to those affected by unemployment. Among the relief provided is assistance to those who have lost health care coverage and are eligible for continuation coverage under the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA); State laws requiring continuation coverage similar to the COBRA rules under the Code; and the continuation coverage requirements of health plans maintained by Federal or State governments. The relief is provided in the form of premium subsidy. ARRA amended the Employee Retirement Income Security Act (ERISA) and the Internal Revenue Code (Code). The terms of the COBRA subsidy are described below.

I. COBRA Premium Subsidy – For a period of up to 15 months, individuals eligible for premium assistance need to pay only 35% of the cost of their COBRA premiums (before it was extended as discussed in Section VIII below, the subsidy was provided only for 9 months). The remaining 65% must be paid by the employer (or any other third party – e.g., the union). The payer of the subsidized portion is later reimbursed via a payroll tax credit.

II. Assistance Eligible Individuals – Individuals who became entitled to continuation coverage under COBRA due to an “involuntary termination” of employment (other than for gross misconduct) on or after September 1, 2008 and before March 1, 2010 (before it was extended as discussed in Section VIII below, the eligibility period ended on December 31, 2009) will receive this subsidy if:

- they elect continuation coverage; and
- their modified adjusted gross income for the taxable year in which the subsidy is received does not exceed \$145,000 (or \$290,000 for joint filers); provided, however, that subsidies paid to taxpayers with incomes between \$125,000 and \$145,000 will be proportionately reduced.

III. Involuntary Termination – ARRA did not define what constitutes an involuntary termination. However, the Internal Revenue Service issued Notice 2009-27 providing details on the implementation of the subsidy. The notice states that the determination of whether a separation from employment is involuntary is made based on all the facts and circumstances. The termination will be deemed involuntary *for purposes of the subsidy* if the facts and circumstances show that the decision to terminate the employment was the independent exercise of the unilateral authority of the employer, other than due to the employee’s implicit or explicit request, where the employee was willing and able to continue performing services.

The examples provided for involuntary terminations include: (i) layoffs, furlough or other suspension of employment; (ii) employee-initiated termination if for good reason due to a material negative change in the employment relationship; (iii) employer action to end employment status while employee is on leave of absence; (iv) retirement when absent said retirement the employer would have terminated the employee’s services; (v) resignation if prompted by a material change in the geographic location of the employment; (vi) lockout initiated by the employer (however, work stoppage as a result of strike initiated by the

employees is not); and (vii) termination elected by the employee in return for a severance package (“buy-out”).

IV. Notice – The COBRA notice that a plan administrator is required to provide to qualified beneficiaries following a qualifying event must also contain information about the subsidy availability, its conditions for eligibility and the penalty described further below. A new notice must also be provided to those individuals who fall within the “Transition Period” described in Section VIII below. The Department of Labor posted model notices in its website.

V. Payment of Subsidy – The entity to which premiums are payable (usually the employer) shall be eligible for a tax credit against payroll tax liabilities in the aggregate amount of the subsidies paid on behalf of its employees. The entity is eligible for the subsidy reimbursement via the tax credit after it has received a reduced premium payment from the assistance eligible individual.

VI. Termination of Subsidy – The subsidy will end on or after the *earlier of*:

- The date on which the 15-month period ends;
- The date following the expiration of the maximum period of continuation coverage required under the applicable COBRA provision (i.e., 18 months for covered individuals);
- The date on which the eligible individual becomes eligible for coverage under any other group health plan (other than coverage consisting only of dental, vision, counseling or referral services, or a combination thereof); or under Medicare benefits of title XVIII of the Social Security Act.

VII. Penalties – An eligible individual who continues to receive the subsidy after he or she is no longer entitled to it (and has failed to notify the entity to which the premiums are paid that his or her eligibility for the subsidy has ended), will be subject to a penalty equal to 110% of the value of the subsidy received after termination of eligibility.

VIII. Extension – The COBRA Subsidy as originally provided by ARRA was extended by the Department of Defense Appropriation Act, 2010 (DDAA) signed into law in December 2009. The DDAA amends certain provisions of ARRA. These amendments are effective retroactively to the date of enactment of ARRA and include:

- Extension of the period of COBRA Subsidy *assistance* for an additional 6 months, increasing the period from 9 months to a total of 15 months.
- Extension of the period of COBRA Subsidy *eligibility* for 2 additional months beyond December 31, 2009 and consequently ending on February 28, 2010.
- Defining a “transition period.”
 - “Transition period” means with respect to any COBRA Subsidy eligible individual, any period of coverage if: (a) such period begins before the

date of the enactment of DDAA, and (b) the premium reduction payable under ARRA would apply to that period pursuant to the DDAA amendment extending the maximum period of the COBRA Subsidy to 15 months.

For example,

- if an individual would have been receiving the COBRA Subsidy on the 10th month through the 15th month of his or her COBRA coverage period had the original period of COBRA Subsidy been 15 months instead of 9 months, and
- the enactment of DDAA occurred on or after the 10th month, but before the 15th month of COBRA coverage, then such individual's "transition period" would run from the 10th month through the 15th month of COBRA coverage.
 - COBRA Subsidy eligible individuals who fall within the "transition period" are allowed to pay past due premiums retroactively and maintain COBRA coverage. Payments of past due periods must be made within 60 days of the enactment of DDAA or within 30 days from the date on which the individual receives the notice mandated by the DDAA.
- Notification. A notice informing assistance eligible individuals of the amendments to ARRA introduced by the DDAA must be sent by the administrator of the group health plan, within 60 days after the enactment of DDAA to individuals who on or after October 31, 2009:
 - were eligible for assistance at any time after such date,
 - experience a qualifying event (termination of employment) relating to COBRA continuation coverage, or
 - were eligible for assistance at any time after such date and did not timely pay the premium for any period of coverage during such individual's "transition period," or paid the full premium, without the benefit of the subsidy reduction.

IX. Additional Rules

- COBRA subsidy is excluded from the individual's gross income.
- If permitted by the employer, COBRA subsidized individuals may change their coverage option to another alternative offered by the plan that costs the same or less than the coverage in place prior to the qualifying event (e.g., change from PPO to HMO coverage).

SEVERANCE ARRANGEMENTS

INTRODUCTION

Many employers provide severance to terminated employees. The reasons why employers provide severance are many and include (1) rewarding employees for years of loyal service; (2) avoiding involuntary reductions in force by providing an incentive for employees to leave voluntarily; (3) taking away the “sting” of an involuntary termination; and (4) perhaps, most importantly from a lawyer’s perspective, avoiding litigation by offering severance in return for a release of claims against the employer. Increasingly, however, such severance arrangements have themselves become the subject of litigation. Such claims are certain to arise with increasing frequency given the reductions in force and other work-force contractions that are beginning to take place and are likely to continue in the wake of the current economic downturn.

A threshold question in any claim involving a severance arrangement is whether that arrangement is an “employee benefit plan” that is covered by the terms of the Employment Retirement Income Security Act of 1974, as amended (“ERISA”). As explained below, the answer to this question in many cases is far from clear, and courts have issued inconsistent, if not outright conflicting guidelines as to when a severance arrangement becomes a covered ERISA plan.

Despite the lack of clear guidance, this question must be grappled with at the outset of any case involving a severance plan or agreement. Whether a claim involves an ERISA plan will impact: (1) the standard of liability; (2) whether the claim is tried to a jury or judge; (3) the appropriate forum for the lawsuit; (4) the potential remedies available to the claimant; and (5) what insurance coverage, if any, applies to the claim.

This paper provides a general overview of current case law and provides guidelines to assist in determining whether a severance agreement is a covered ERISA plan. Finally, the paper briefly explores and discusses the strategic considerations and ramifications of ERISA coverage as applied to severance plans.

SECTION 1 **PREREQUISITE TO ERISA COVERAGE ... A “PLAN”**

In general, ERISA applies to any “employee benefit plan” that is established or maintained by any employer or employee organization engaged in commerce or in any industry or activity affecting commerce, or by both an employer and an employee organization. 29 U.S.C. §1003(a). The term “employee benefit plan” is defined as either an “employee welfare benefit plan” or an “employee pension benefit plan” or a plan which is both a welfare and a pension plan. 29 U.S.C. §1002(3).

ERISA defines “employee welfare benefit plan” or “welfare plan” as:

any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or an employee organization, or by both, to the extent that such plan, fund, or program was established or maintained for the purpose of providing for its participants or their beneficiaries, through the purchase of insurance or otherwise, (A) medical, surgical, or hospital care or benefits, or benefits in the event of sickness, accident, disability, death or unemployment, or vacation benefits, apprenticeship or other training programs, or day care centers, scholarship funds, or prepaid legal services, or (B) any benefit described in §302(c) of the Labor Management Relations Act, 1947. . .

29 U.S.C. §1002(1). It is well-established that severance benefits can be “welfare benefits” under ERISA’s definition. See, e.g., Donovan v. Dillingham, 688 F. 2d 1367, 1371 (11th Cir. 1982).

Though ERISA purports to define “employee benefit plan,” it does so in a tautological manner, referring in the definition itself to the word “plan,” without further guidance. Courts struggled with this lack of guidance on many occasions, until finally, the now commonly-used definition of “plan” was formulated by the Eleventh Circuit in the Donovan v. Dillingham case. Id. The Donovan court used a four-factor test in making its determination as to whether or not the plan at issue in the case was an “ERISA plan.” The court described its test in the following way:

In determining whether a plan, fund or program (pursuant to a writing or not) is a reality a court must determine whether from the surrounding circumstances a reasonable person could ascertain the intended benefits, beneficiaries, source of financing, and procedures for receiving benefits. . . To be an employee welfare benefit plan, the intended benefits must be health, accident, death, disability, unemployment or vacation benefits, apprenticeship or other training programs, day care centers, scholarship funds, prepaid legal services or severance benefits; the intended beneficiaries must include union members, employees, former employees or their beneficiaries; and an employer or employee organization, or both, and not individual employees or entrepreneurial businesses, must establish or maintain the plan, fund, or program.

Id. at 1373.

The Donovan court made clear that an ERISA plan need not be formal, nor written. Id. at 1372. The court noted that though ERISA requires that plans be maintained pursuant to a written instrument, that is merely a responsibility of the plan administrator and fiduciary, and not a prerequisite to coverage under the Act. Id. “Because the policy of ERISA is to safeguard well-being and security of working men and women and to apprise them of their rights and obligations under any employee benefit plan. . .it would be incongruous for persons establishing

or maintaining informal or unwritten employee benefit plans. . .to circumvent the Act merely because an administrator or other fiduciary failed to satisfy reporting or fiduciary standards.” Id. Although an ERISA plan may exist even in the absence of formal, written plan documents, the informal plan must actually be in existence; the mere decision or statement of intention to create an employee benefit plan is not actionable under ERISA. See, e.g., Elmore v. Cone Mills Corp., 23 F.3d 855, 861 (4th Cir. 1994); James v. Natl. Business Sys., Inc., 924 F.2d 718 (7th Cir. 1991). In addition, an informal plan may exist in addition to a formal plan as long as the informal plan independently meets all of the factors outlined in Donovan. See Henglein v. Informal Plan for Plant Shutdown Benefits for Salaried Employees, 974 F.2d 391, 400 (3^d Cir. 1992).

SECTION 2

WHEN ARE SEVERANCE PLANS CONSIDERED “ERISA PLANS”?

The leading case on the issue of when a severance arrangement constitutes an ERISA plan is Fort Halifax Packing Co. v. Coyne, 482 U.S. 1, 107 S. Ct. 2211, 96 L. Ed. 2d 1 (1987). In that case, the Supreme Court held that a Maine statute that required employers in Maine to provide a one-time severance payment in the event of a plant closing did not create an ERISA plan. The Court recognized that though the policy behind ERISA is to avoid a “patchwork scheme of [state-by-state] regulation [which] would introduce considerable inefficiencies in benefit program operation” and to “bring a measure of uniformity” into the area of benefits law, certain benefits would nevertheless not rise to the level of a “plan.” Id. at 11. The Court reasoned that:

The requirement of a one-time, lump-sum payment triggered by a single event requires no administrative scheme whatsoever to meet the employer’s obligation. The employer assumes no responsibility to pay benefits on a regular basis, and thus faces no periodic demands on its assets that create a need for financial coordination and control. Rather, the employer’s obligation is predicated on a single occurrence that may never materialize. . . . To do little more than write a check hardly constitutes the operation of a benefit plan.

Id. at 12.

Since Fort Halifax, courts have been faced with the difficulty of measuring the degrees by which a program of benefits requires an “administrative scheme” and “financial coordination and control.” In determining whether or not a “separate, ongoing administrative scheme” exists, and therefore, whether the program at issue is an ERISA plan, most courts have looked at the following four factors:

- whether the payments are one-time, lump sum payments, or continuous, periodic payments;
- whether the employer is obligated over a prolonged or a limited time period;

- whether the severance payments are triggered by a single event or are continuous payments to be made generally to terminated employees; and
- whether the severance plan requires the employer to engage in a case-by-case review of employees to determine their particular eligibility based on the applicable criteria.

The last two factors—employer discretion and ongoing employer obligation—are frequently determinative. See, e.g., Kolkowski v. Goodrich Corp., 448 F.3d 843, 848 (6th Cir. 2006); Kosakow v. New Rochelle Radiology Assocs., P.C., 274 F.3d 706, 737 (2^d Cir. 2001). Therefore, in general, when looking at whether or not a severance pay plan or practice would constitute an “ERISA plan,” it is important to review the level of managerial discretion that goes into the determination of eligibility for benefits, as well as the longevity of the employer obligation.

Examples of severance plans and practices that have fallen on the ERISA-side of the fence included the following:

- A one-time lump sum payment of two times an employee’s weekly compensation for each year of employment was an ERISA plan. Simas v. Quaker Fabric Corp., 6 F.3d 849 (1st Cir. 1993).
- A severance program that provided payments based on length of employment and prospects of reemployment, with payments made only if employee was involuntarily terminated and made a good faith effort to obtain new similar position was an ERISA plan. Schonholz v. Long Island Jewish Med. Ctr., 87 F.3d 72 (2^d Cir. 1996).
- A severance protection plan that is triggered by diminution of duties or loss of benefits following change in control, with one-year period for making demand for benefits and mandatory notification by employer of right to receive benefits was an ERISA plan. Bowles v. Quantum Chemical Co., 266 F.3d 622 (7th Cir. 2001).
- A retention program that offered employees severance benefits if neither the company nor the buyer offered “substantially equivalent” employment to the employee following termination of the employee was an ERISA plan. Bogue v. Ampex Corp., 976 F.2d 1319 (9th Cir. 1993).
- A policy manual providing that terminated employees would “receive appropriate severance pay where applicable” was found to be an ERISA plan because severance pay was offered without any apparent date restriction, could reasonably be seen by employees as an ongoing commitment, and the employer would have to determine the amount owed in each individual case. Kosakow, 274 F.3d at 737.

Severance plans that have been held not to implicate ERISA included the following:

- A golden parachute arrangement that paid a lump sum of three times the employee's highest annual compensation for the past three years, plus three years of continued benefits was not an ERISA plan. Fontenot v. NL Ind., Inc., 953 F.2d 960 (5th Cir. 1992).
- A buyout plan paying departing employees a lump sum of \$75,000 and one year of continued benefits to be administered under the company's pre-existing benefit plans was not an ERISA plan. Angst v. Mack Trucks, Inc., 969 F.2d 1530 (3^d Cir. 1992).
- An offer of 60 days additional pay upon termination was not an ERISA plan. James v. Fleet/Norstar Fin. Group, 992 F.2d 463 (2^d Cir. 1993).
- A lump sum payment of 2.99 times an employee's annual compensation if terminated or resigned within one year of a hostile takeover was not an ERISA plan. Kulinski v. Medtronic Bio-Medicus, Inc., 21 F.3d 254 (8th Cir. 1994).
- A voluntary termination plan that paid employees a lump sum payment based on years of seniority plus six months continued health coverage was not an ERISA plan, even though there was a rehire consequence in the plan that limited an employee who received benefits under the plan from again voluntarily terminating under the plan following a rehire until the employee had attained at least five additional years of seniority with the company. Anderson v. Chrysler Corp., 1998 U.S. Dist. LEXIS 23107 (N.D. Ala. Dec. 21, 1998).
- A golden parachute plan that paid severance to the nine key employees who were chosen to participate, if they were terminated without cause within twelve months of the merger or resigned for good reason, and if they did not receive comparable employment, as long as they were satisfactory employees that had complied with prior agreements (including non-compete agreements) and as long as they signed a release was not an ERISA plan. Lettes v. Kinam Gold Inc., 2001 U.S. App. LEXIS 949 (10th Cir. Jan. 23, 2001).
- A severance bonus based on tenure and calculated at the rate of two-and-a-half weeks' pay for each of the first ten years of service plus two weeks for each additional year, up to a maximum of 78 weeks' salary (for 37 years of service) was not an ERISA plan. O'Connor v. Commonwealth Gas Co., 251 F.3d 262 (1st Cir. 2001).

As you can see from the above examples, the line-drawing that the courts engage in when determining whether a severance arrangement is an ERISA plan is far from precise. As a general rule of thumb, however, the more “administration” or “discretion” that is required in calculating or determining eligibility for severance, the more likely it will be that the arrangement at issue is an ERISA plan.

SECTION 3 **SPECIAL CONSIDERATIONS**

A. ONE-MAN SEVERANCE PLANS

For a time, it was argued that ERISA did not apply to “one man plans,” or benefit arrangements that involved only a single employee. Such a rule would exclude benefits under individual separation and release agreements from ERISA coverage. The courts have, however, rejected this argument.

There is nothing in ERISA’s language or administrative history that would preclude a finding that an ERISA plan existed where only one employee was covered. See Cvelbar v. CBI Illinois, Inc., 106 F.3d 1368, 1375-1376 (7th Cir. 1997). In Cvelbar, the Seventh Circuit held that as long as the program at issue (a retention agreement between Mr. Cvelbar and his employer that in the event of voluntary or involuntary termination, the company would provide him with severance benefits) meets the other requirements of an ERISA plan, “namely, an ongoing administrative scheme and reasonably ascertainable terms– the program does not fall outside the ambit of ERISA merely because it covers only a single employee.” Id. at 1376.

Similarly, in Biggers v. Wittek Ind. Inc., 4 F.3d 291 (4th Cir. 1993), the Fourth Circuit noted that there is nothing in ERISA’s definitions of “employee welfare benefit plan” nor “employee benefit” that would suggest that the number of employees covered is a determinative factor. Biggers, 4 F.3d at 297. Therefore, it is important to remember that simply because the severance arrangement covers a single employee does not remove it from ERISA’s reach.

B. ESTOPPEL

Another issue that may arise related to severance arrangements is the possibility that an aggrieved employee may raise a claim of estoppel in order to recover benefits. This argument most often exists when an employee argues that his employer misrepresented his eligibility for benefits or the availability of certain severance payments, and the employee reasonably relied on that inducement to his detriment in making his retirement decisions.

Courts may enforce a “promise” of benefit payments under an ERISA plan if an employee can prove that the employer made a promise or written misrepresentation on which he detrimentally relied, the reliance was reasonable, and that he would be damaged if the promise is not enforced. See, e.g., Bock v. Computer Assocs. Intl., Inc., 257 F.3d 700 (7th Cir. 2001). However, an ERISA plan may not be modified by an oral promise, and estoppel may not be used to create coverage contrary to the terms of a written ERISA plan.

SECTION 4
IF ERISA APPLIES, WHAT ARE THE RISKS (AND REWARDS)?

There are two main areas of exposure with respect to lawsuits arising out of ERISA-governed severance plans. First, participants may sue to recover benefits allegedly due them under the terms of the plan. Second, plan fiduciaries may be sued for breach of ERISA's fiduciary duty requirements.¹

A. BENEFIT CLAIMS

A claim for benefits under an ERISA plan is analogous to a state-law breach of contract claim. These claims arise under ERISA Section 502(a)(1)(B), and must be brought by either a participant or a beneficiary to recover benefits due under the terms of the plan, to enforce rights under the plan, or to clarify rights to future plan benefits. In general, a participant or beneficiary is required to exhaust the plan's internal administrative remedies before resorting to federal court on his or her claim.

B. BREACH OF FIDUCIARY DUTY CLAIMS

The most common breaches of fiduciary duty under ERISA Section 503 are (1) failure to follow the terms of the plan, and (2) making a material misrepresentation as to a participant's eligibility for benefits under a plan or participation in the plan.

1. WHO ARE FIDUCIARIES?

In order to understand the risks of breaches of fiduciary duty, it is essential to first understand who is a fiduciary and the obligations of a fiduciary. ERISA states the following with respect to who is a fiduciary under the law: "[A] person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee . . . , or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan. 29 U.S.C. §1002(21)(A).

An ERISA fiduciary is required to "discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and. . . for the exclusive purpose of. . . providing benefits to participants and their beneficiaries. . . in accordance with the documents and instruments governing the plan. . ." 29 U.S.C. §1104(a)(1). In short, a fiduciary is required to act in the best interests of the plan participants and administer the plan according to its terms. Employers are often administrators of benefit plans, and thus, are the most common ERISA fiduciary.

¹ The other area of exposure generally arises under ERISA Section 510 for alleged interference with the attainment of benefits under an ERISA plan. Such claims rarely, if ever, arise in connection with severance plans, however. Further, severance benefit plans are exempt from the more stringent requirements of ERISA, such as its vesting, participation, and funding requirements. *Joanou v. Coca-Cola Co.*, 26 F.3d 96 (9th Cir. 1994).

An employer can wear many hats, however. All decisions made by the employer are not covered by ERISA's fiduciary constraints. It is only when an employer is wearing its fiduciary hat that it is subject to those rules. For example, companies that "alter the terms of a plan do not fall into the category of fiduciaries." Lockheed Corp. v. Spink, 517 U.S. 882, 890 (1996). "Employers or other plan sponsors are generally free under ERISA, for any reason at any time, to adopt, modify, or terminate welfare plans." Curtiss-Wright Corp. v. Shoonejongen, 514 U.S. 73, 78 (1995) (citing Adams v. Avondale Ind., Inc., 905 F.2d 943, 947 (6th Cir. 1990)). In addition, when an employer makes decisions about the design of a severance plan, it functions as an employer and not an administrator and thus is not acting as a fiduciary. See Noorily v. Thomas & Betts Corp., 188 F.3d 153, 159 (3rd Cir. 1999). Finally, to the degree the plan gives the administrator discretion to determine benefits under the plan, it is not acting as a fiduciary when it makes determinations under the plan's terms that affect employees' eligibility for benefits. Id.

2. WHAT ARE THE RISKS TO FIDUCIARIES?

As discussed above, a fiduciary breach may occur when a fiduciary either fails to pay benefits under the terms of the plan or makes a material misrepresentation regarding the plan. As to the latter, the difficulty arises in determining what obligation an employer-fiduciary has to inform its employees about its decisions regarding severance plans.

Under the "serious consideration" test, there is no fiduciary obligation to disclose the existence or contemplated existence of an ERISA plan or any contemplated changes to an existing plan until such plan or such changes come under serious consideration. See Barnes v. Lacy, 927 F.2d 539 (11th Cir. 1991). In order to have a claim for breach of fiduciary duty, the plan must have been under serious consideration at the time the alleged misrepresentation was made. But even an employer's serious consideration of a plan does not in and of itself implicate ERISA's fiduciary duties; it is only when the employer communicates with an employee about the plan. See Bins v. Exxon Co. U.S.A., 220 F.3d 1042, 1053 (9th Cir. 2000). And, an ERISA fiduciary does not have an affirmative duty prior to final approval of the plan to volunteer information about the plan to employees who have not specifically asked about it. Id. The serious consideration test has been described as "(1) a specific proposal (2) is being discussed for purposes of implementation (3) by senior management with the authority to implement the change." Fischer v. Philadelphia Electric Co., 96 F.3d 1533 (3^d Cir. 1996), *cert. denied*, 137 L. Ed. 2d 329, 117 S. Ct. 1247 (1997).

However, when a participant makes an allegation of affirmative misrepresentation by an employer-fiduciary, some courts have looked to a less deferential standard to analyze the materiality of the employer's allegedly misleading statements. The factors include "how significantly [the false] statement misrepresented the present status of internal deliberations regarding future plan changes, the special relationship of trust and confidence between a plan fiduciary and beneficiary, . . . and the specificity of the assurance." See Vartanian v. Monsanto Co., 131 F.3d 264, 269 (1st Cir. 1997) (citing Ballone v. Eastman Kodak Co., 109 F.3d 117, 125 (2nd Cir. 1997)); see also Hockett v. Sun Co., Inc., 109 F.3d 1515 (10th Cir. 1997). But at least one court has interpreted this analysis to apply only to deliberations regarding voluntary severance plans, in which an employee has a right to choose to participate. See Winkel v. Kennecott Holdings Corp., 48 F. Supp. 2d 1294 (C.D. Utah, 1999) (policy behind serious

consideration test does not apply to involuntary severance plans, in which employees do not choose to participate, and because of lack of appropriate remedy for alleged breach).

Passive behavior, on the other hand, has been held to give rise to a claim of breach of fiduciary duty only when the fiduciary fails to give a beneficiary material information regarding a plan and the fiduciary's silence is misleading. See, e.g., Watson v. Deaconess Waltham Hosp., 298 F.3d 102, 115 (1st Cir. 2002); Becker v. Eastman Kodak, 120 F.3d 5 (2nd Cir. 1997); Chojnacki v. Georgia-Pacific Corp., 108 F.3d 810, 817 (7th Cir. 1997); Bixler v. Central Penn. Teamsters Health & Welfare Fund, 12 F.3d 1292 (3rd Cir. 1993); Eddy v. Colonial Life, 919 F.2d 747 (D.C. Cir. 1990).

3. WHAT TYPE OF RELIEF IS AVAILABLE?

In Varity Corp. v. Howe, the Supreme Court held that ERISA Section 502(a)(3) authorizes lawsuits for *individual equitable relief* for breaches of fiduciary duty. Varity Corp. v. Howe, 516 U.S. 489, 116 S. Ct. 1065, 134 L. Ed. 2d 130 (1996) (emphasis added). However, the Court was clear that when relief is available to a participant by virtue of another provision of ERISA, a claim under Section 502(a)(3) would not be "appropriate." Varity, 116 S. Ct. at 1079. Therefore, a plaintiff's claim for breach of fiduciary duty may not stand if he also has a claim for wrongfully denied benefits under the terms of the plan by virtue of ERISA Section 502(a)(1)(B). Id.

In general, in accordance with the Varity decision, courts have allowed individual recovery only the form of equitable relief for a successful claim for breach of fiduciary duty. Recovery of the benefits claimed under a plan, however, is not an appropriate remedy for breach of fiduciary duty. See, e.g., Kulesza v. New York Univ. Med. Ctr., 129 F. Supp. 2d 267 (S.D.N.Y. 2001).

SECTION 5 **WHY DOES IT MATTER IF A SEVERANCE** **ARRANGEMENT IS AN ERISA PLAN?**

A. PREEMPTION OF STATE LAW

The determination of whether or not a severance arrangement is an ERISA plan is critically important because ERISA generally preempts all state laws that would otherwise apply to claims involving an ERISA severance plan. From the standpoint of a potential defendant or insurer, this has both benefits and drawbacks. On the one hand, if the benefit arrangement is considered to be covered by ERISA, the standard of review would be more deferential towards the plan administrator, the right to trial by jury would be limited, the remedies available to a successful plaintiff may be less than if the arrangement were governed by state law, and the case can be removed to federal court. On the other hand, ERISA does allow prevailing plaintiffs to recover attorneys fees in many situations, a remedy that is not typically available in a state law breach of contract action.

Section 514 of ERISA contains broad preemptive language. That section states that the provisions of Title I of ERISA “shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan. . .” 29 U.S.C. §1145(a). The Supreme Court has held that a state law “relates to” an ERISA plan “if it has a connection with or reference to such a plan.” Shaw v. Delta Air Lines, Inc., 463 U.S. 85, 97, 77 L. Ed. 2d 490, 103 S. Ct. 2890 (1983).

Even laws impacting benefit agreements that in and of themselves would not constitute ERISA plans may be preempted, if the benefits provided under the agreements refer to an ERISA plan. For example, in Dranchak v. Akzo Nobel Inc., 88 F.3d 457 (7th Cir. 1996), the Seventh Circuit found that state law claims relating to a letter agreement that gave the recipient employee extra years of pension credit and extended medical coverage were preempted by ERISA. The court reasoned that because the letter agreements told the plan administrator how much to disburse to the employee from the various ERISA-governed pension and health plans, the state law claims to enforce the letter agreements were preempted by federal law. Id. at 459. The court concluded that “[r]ules governing payment to participants from pension and welfare plans necessarily “relate to” those plans,” and therefore must be preempted. Id.

B. STANDARD OF REVIEW

The judicial determination as to whether or not a plan is covered by ERISA affects the level of scrutiny and degree of discretion the court will use in scrutinizing decisions made by an employer or administrator under the plan. If a severance arrangement is not an ERISA plan, state law will govern, and the arrangement usually will be subject to a traditional contract-law analysis, where the contract is construed against the drafter and the interpretation of the employer receives no additional deference.

In contrast, if the severance arrangement is covered by ERISA, as long as the plan at issue contains language that is sufficient to confer discretion on the plan administrator to determine benefits under the plan, the court will use the “arbitrary and capricious” standard of review— an extremely deferential standard— in examining the administrator’s decision to either grant or deny benefits. See Firestone Tire & Rubber Co. v. Bruch, 489 U.S. 101, 109 S. Ct. 948, 103 L. Ed. 2d 80 (1989). In short, under the arbitrary and capricious standard, the plan administrator’s decision will not be second-guessed by the court unless it is unreasonable, and not merely incorrect. See, e.g., Herzberger v. Standard Ins. Co., 205 F.3d 327, 329 (7th Cir. 2000).

C. AVAILABILITY OF JURY TRIALS

Another issue to consider in weighing the pros and cons of ERISA-status is the extremely limited availability of jury trials for claims under ERISA. In most cases, there is no right to a jury trial for claims under ERISA. Most courts have held that because ERISA’s remedial provisions are based on the law of trusts, they are equitable in nature and therefore are not appropriately tried to a jury (unless both parties agree to trial by jury). There are some courts that have permitted jury trials in suits to recover benefits under an ERISA plan, if the suit can be characterized as “legal,” rather than “equitable.” This analysis is limited, however, and most circuits have characterized severance benefit claims as equitable and not triable by jury. See,

e.g., Eichorn v. AT&T Corp., 484 F.3d 644, 655 (3^d Cir. 2007); Adams v. Cyprus Amax Minerals Co., 149 F.3d 1156 (10th Cir. 1998); Tischmann v. ITT/Sheraton Corp., 145 F.3d 561 (2^d Cir. 1998); Nevill v. Shell Oil Co., 835 F.2d 209 (9th Cir. 1987). Given the unpredictable and, at times, unfavorable nature of jury awards, this may often be a distinct advantage for defendants.

D. REMEDIES

As discussed above, a determination that a severance arrangement is covered by ERISA may lead to the preemption of state laws, many of which may be unfavorable to the employer. For example, the state of Illinois requires all employers to pay wages due to their employees (including wages, salaries, earned commissions, earned bonuses, and the monetary equivalent of earned vacation and earned holidays) no later than the next usual payday following the employee's termination of employment. 820 ILCS 115/5. Failure to do so may result in a penalty of 1% per calendar day to the employer for each day of delay in paying owed wages, up to an amount equal to twice the sum of unpaid wages due to the employee. 820 ILCS 115/14. The enforcement provision is mandatory; there is no good faith exception.

So, if an Illinois plaintiff brought a claim for benefits allegedly owed under a severance pay plan that was not determined to be covered by ERISA, the state's wage statute would likely apply, and the employer would potentially be liable for damages equal to the full amount of owed wages. On the other hand, if the severance pay plan at issue was an ERISA plan, Section 514 would mandate preemption of the wage claim as to the severance payments, and the maximum benefits that could be owed by the employer would be limited to the benefits allegedly owed under the terms of the plan.

In contrast, the remedies available under ERISA for a successful claim for benefits is limited to the amount of the benefits. The court also has discretion to award attorneys fees to the prevailing party in an ERISA action (as discussed in Part E. below). Moreover, unlike state law, ERISA generally does not provide for awards of punitive damages.

E. ATTORNEYS' FEES

ERISA specifically provides that a prevailing party may recover its attorneys fees. Generally, this is not a remedy that would be available under a state law breach of contract claim unless the contract specifically provided for an award of fees. Courts have discretion as to whether or not to award attorneys' fees to the prevailing party, and in doing so, generally look at factors such as (1) the degree of the opposing parties' culpability; (2) the ability of the opposing party to satisfy a fee award; (3) whether a fee award would be a deterrent to others; (4) whether others in the ERISA plan would benefit from the decision; and (5) the relative merits of the parties' positions.

While there is a slight bias in favor of awarding fees to prevailing plaintiffs and against awarding fees to prevailing defendants, courts exercise far more discretion in awarding fees in ERISA cases than in other fee shifting cases, such as discrimination claims under Title VII. More often than not, this discretion results in each party paying its own attorneys' fees, rather than a significant fee award to the prevailing party.

CONCLUSION

The issue of whether or not a severance arrangement constitutes an ERISA plan depends on the nature of the arrangement itself. There are no bright-line tests, which gives the employer the opportunity to strategize and consider whether or not they will be benefitted by creating certain types of arrangements. Factors that should be considered include: the standard of review, availability of jury trial, preemption of state law, attorneys' fees and remedies available. While it may be frustrating at times, the law in this area gives employers a great deal of latitude in managing their exposure on many critical issue.