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## Identifying Whether Your Severance Plan Is an ERISA Plan and Understanding ERISA’s Consequences

Many companies with severance “plans” have considered the employment law implications of such plans. However, fewer employers have considered the employee benefit implications that can apply to severance plans, in part because severance plans are subject to the Employee Retirement Income Security Act of 1974 (“ERISA”) in limited circumstances. It is important to identify when ERISA applies: an employer that maintains a severance plan that is subject to ERISA but fails to follow ERISA’s requirements may be subject to potential penalties, including monetary and even criminal penalties.

Among other things, ERISA defines an employee benefit plan as “any plan, fund, or program... established or maintained by an employer ... for the purpose of providing for its participants or their beneficiaries...any benefit described in Section 186(c)...” Among the benefits described in Section 186(c) are severance benefits.

Prior cases provide that whether a severance plan fits the definition of “employee benefit plan” above is based on the facts and circumstances of the plan and how the plan is designed and administered. The main factors in determining whether the facts and circumstances indicate the severance plan is subject to ERISA are:

- Whether the employer is required to exercise discretion in determining the eligibility to receive severance benefits; and
- Whether the severance payments are paid based on an “ongoing administrative scheme.” Factors for determining whether there is an ongoing administrative scheme include:
  - whether the payments are one-time lump sums or continuous;
  - whether the employer undertook any long-term obligation with respect to the payments;
  - whether the severance payments come due upon the occurrence of a single, unique event or anytime the employer terminates employees; and
  - whether the severance arrangement under review requires the employer to engage in a case-by-case review of employees.

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- ERISA imposes a number of requirements on severance plans subject to it, including (for example):
  - The plan must be in writing.
  - The plan must include a claims procedure.
  - The plan must file an annual Form 5500, unless the plan has fewer than 100 participants.
  - To calculate the number of participants, the employer must count each employee who could be entitled to a benefit under the plan, not just those who actually receive a benefit.
  - Participants must be provided with a summary plan description of the plan.

Failing to follow ERISA's requirements can result in monetary penalties for failing to provide a summary plan description or failing to file annual reports, and criminal penalties for willful violations of ERISA's reporting and disclosing retirements.

It is not all doom and gloom, as there are several benefits a severance plan gains by being subject to ERISA. For example, with a written plan document, an employer can easily make changes to the plan, as opposed to being held to a "past practice" standard. In addition, employees will be subject to a claims procedure under which an employer's decision will be overturned only if the employer acts in an "arbitrary and capricious" manner. This is a significant benefit to employers if a dispute arises. ERISA litigation is also typically done in federal courts which tend to favor employers. For these (and other) reasons, some employers purposely choose to make their severance plans subject to ERISA.

As described above, a severance plan that is subject to ERISA will have significant impacts on plan administration and its treatment under the law. If you would like to review your severance plan for ERISA impacts, redesign your severance plan to avoid (or be subject to) ERISA, or set up a new severance plan, please contact a member of the Kutak Rock [Employee Benefits and Executive Compensation practice group](#).

