

EIGHTH CIRCUIT CLARIFIES THE SCOPE OF ERISA'S APPLICATION TO SEVERANCE ARRANGEMENTS

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The Eighth Circuit's recent decision in *Dakota, Minn. & E. R.R. Corp. v. Schieffer* (*Schieffer II*), No. 12-1807, 2013 WL 1235235 (8th Cir. Mar. 28, 2013), offers new insight into the circumstances under which severance benefits provided under an executive's employment contract are governed by ERISA. The opinion clarifies that ERISA does not govern contractual obligations in an executive employment contract that are not provided under an ERISA plan and, even where amount of payments are made by reference to the terms of an ERISA plan, the arrangement does not "relate to" an ERISA plan.

Schieffer concerned a dispute over severance benefits after the employer ("DM&E") terminated its CEO in anticipation of a merger. Under the employment agreement, DM&E had agreed to continue providing Schieffer benefits for three years following his severance payment. These benefits, as described in the employment agreement, included "all employee health, welfare and retirement benefits plans and programs made available generally to senior executives,' and, if Schieffer became ineligible to participate, 'whether by law or the terms thereof,'" DM&E "would make 'a cash payment equal to' what it would have contributed if he participated" in the plan. *Id.* at *3. Schieffer filed a demand for arbitration, seeking among other things double-damages under a state wage statute that would be preempted if ERISA applied. DM&E responded by filing a declaratory judgment action in federal court to enjoin the arbitration. The arbitration demand had alleged that DM&E had breached obligations under the employment agreement by (1) terminating health insurance coverage prematurely; (2) failing to pay life and disability insurance coverage for the full contractual period; (3) miscalculating retirement benefits; and (4) failing to pay "vacation accruals and banked vacation cash compensation payable to terminated employees under the employment benefit programs." *Id.* at *2. Because neither the Declaratory Judgment Act nor the Federal Arbitration Act (which Schieffer might have used to compel arbitration) is jurisdictional, the federal court could not hear the case unless the dispute arose under ERISA. Thus, DM&E contended that the demand sought benefits covered by the company's ERISA plan. Note that neither the Eighth Circuit nor this blog entry addresses the potential tax issues associated with this type of arrangement (e.g., under Code Section 409A and/or 105(h)). Be on the lookout for a blog entry

highlighting the tax consequences associated with the continuation of executive health and welfare benefits post-separation from service.

In *Schieffer I*, the Eighth Circuit court held that an individual employment agreement providing severance benefits to a single executive is not an ERISA welfare benefit plan within the meaning of the statute and, therefore, that Schieffer's benefits were not provided under an ERISA plan. *Dakota, Minn. & E. R.R. v. Schieffer (Schieffer I)*, 648 F.3d 935, 938 (8th Cir. 2011). The analysis, however, did not end there because, as the Eighth Circuit noted, ERISA preemption extends to all state laws that "relate to" an employee benefit plan. See 29 U.S.C. § 1144(a). Schieffer's employment agreement provided that DM&E would "continue to provide [him] the Employee Benefits described in section 3(c) of this Agreement for a period of not less than three years from the date on which the Severance Payment is paid in full" *Schieffer II*, 2013 WL 1235235, at *3. The cross-referenced section 3(c) provided that Schieffer and his dependents would participate in "all employee health, welfare, and retirement benefit plans and programs made available generally to senior executives" and, if he became ineligible to participate, then DM&E would make "a cash payment equal to" what it would have contributed if he participated. According to the Eighth Circuit, if Schieffer's arbitration demands were demands for payment under an ERISA benefit plan, then to that extent all state law remedies are preempted and the district court would have subject matter jurisdiction. *Id.* at *2. On the other hand, if Schieffer's demands were pursuant to "a free-standing single-employee contract that simply pegged DM&E's payment obligations to amounts that would have been due under ERISA plans, there [was] no preemption" of state law remedies asserted in the demand for arbitration." *Id.* (quoting *Schieffer I*, 648 F.3d at 938)) (emphasis added). The Eighth Circuit remanded to the district court for a determination of this issue.

On remand, the district court determined that the provisions merely "pegged" the former CEO's benefits to amounts due under the actual ERISA plan without providing coverage under the plan itself. *Id.* at *1. This decision set the stage for DM&E's appeal and *Schieffer II*. In *Schieffer II*, the Eighth Circuit identified two circumstances under which the employment agreement might create benefits due under an ERISA plan. First, the agreement could be an "amendment" to an ERISA plan. *Id.* at *3. Second, the agreement might be a "promise that ERISA plan benefits will be paid if a future contingency occur[red]." *Id.* (quoting *Johnson v. U.S. Bancorp.*, 387 F.3d 939, 942 (8th Cir. 2004)).

The Eighth Circuit found that neither of these exceptions applied. To begin, there was no evidence that the agreement amended an ERISA plan, and in fact, the agreement concerned post-termination payments that could only occur when Schieffer was no longer a participant in the company's plans. Next, this was a "free-standing agreement" and not a promise to pay benefits upon a future contingency. Although the benefits were measured by the ERISA plans, two considerations prevented the necessary link to the ERISA plans themselves. First, DM&E had not indicated that the funds came from anywhere other than its general assets (i.e., they had not alleged that the benefits

were funded by an ERISA plan). *Id.* Second, DM&E had not alleged that the payment would affect the administration of its ERISA plans or “threaten ERISA’s goal of uniformity in the administration of plan benefits.” *Id.* Accordingly, the Eighth Circuit concluded that Schieffer’s arbitration demand did not seek benefits “due under” an ERISA plan, and the federal court lacked subject matter jurisdiction over the dispute. *Id.* As a corollary, ERISA could not preempt Schieffer’s state law claims, including his request for double damages.

Following the Eighth Circuit’s decision in *Schieffer II*, consider the following:

1. Cash payments calculated by reference to benefits provided under an ERISA plan do not “relate to” an ERISA plan for purposes of determining ERISA preemption issues.
2. Attempts to bring executive severance payments and benefits within the scope of ERISA raise a variety of tax and benefits issues that require careful consideration.

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