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NOTE

SEVERANCE PAY CLAIMS AFTER A SALE OF ASSETS: ERISA SWEEPS THE FIELD

The Employee Retirement Income Security Act of 1974 (ERISA)¹ was enacted by Congress as a uniform remedy for the inadequate protection afforded by state law to employees participating in private benefit plans.² ERISA is a broad and complex

¹ Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, § 1, 88 Stat. 829 (1974) (codified in sections of Titles 5, 18, 26, 29, 31, & 42 U.S.C.) [hereinafter cited as ERISA].

² See H.R. REP. NO. 533, 93d Cong., 2d Sess. 4, reprinted in 1974 U.S. CODE CONG. & AD. NEWS 4639, 4641 [hereinafter cited as *House Report*]. Although private employee benefit plans expanded in number and scope of capital prior to the enactment of ERISA, their rapid growth was not matched by a corresponding growth in their regulation. See Hutchinson & Ifshin, *Federal Preemption of State Law Under the Employee Retirement Income Security Act of 1974*, 46 U. CHI. L. REV. 23, 24-25 (1978).

Prior to ERISA, the regulatory mechanisms for these plans were built upon state contract and trust principles. See Herbert, *Investment Regulation and Conflicts of Interest in Employer-Managed Pension Plans*, 17 B.C. INDUS. & COM. L. REV. 127, 129 (1976). However, state court interpretations of these principles tended to be narrow, and limited the recovery capability of employees by strictly interpreting pension provisions with an eye toward "parochialism" rather than equitable relief. *Id.*; see, e.g., *Burns v. Winkler*, 221 Ga. 285, 286, 144 S.E.2d 337, 338-39 (1965) (plaintiff-employee held to have contract right only, not beneficiary privileges, as against employer); *Whitley v. Mammoth Life & Accident Ins. Co.*, 273 S.W.2d 42, 43 (Ky. 1954) (plaintiff-employee held to have no standing to sue trustees of pension plan). Thus, determining that "the continued well-being and security of millions of employees and their dependents are directly affected" by private pension plans, ERISA § 2(a), 29 U.S.C. § 1001(a) (1982), Congress enacted the more comprehensive ERISA. ERISA § 2(b), 29 U.S.C. § 1001(b) (1982).

ERISA differentiates between an "employee welfare benefit plan," ERISA § 3(1), 29 U.S.C. § 1002(1) (1982), and an "employee pension benefit plan," ERISA § 3(2), 29 U.S.C. § 1002(2) (1982). Pension plans typically involve a promise by an employer to pay a deferred fixed benefit, and include retirement benefits and profit sharing plans. ERISA § 3(2)(A), 29 U.S.C. § 1002(2)(A); see also Comment, *The Employee Retirement Income Security Act of 1974: Policies and Problems*, 26 SYRACUSE L. REV. 539, 545-46 (1975). A "welfare benefit plan" is defined by ERISA to include:

[A]ny plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the

statute,³ designed to promote employee interests by creating a federal cause of action for recovery of funds due under employer benefit plans.⁴ The Congressional objective of creating uniformity in the area of employee benefits is achieved through the federal preemption of all state laws that "relate to" an employee benefit plan.⁵ ERISA also creates standards of fiduciary conduct for those

extent that such plan, fund, or program was established or is 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 (B) any benefit described in section 186(c) of this title [section 302(c) of the Labor-Management Relations Act] (other than pensions on retirement or death, and insurance to provide such pensions).

ERISA § 3(1), 29 U.S.C. § 1002(1) (1982).

³ See Lurie, *Reforming ERISA: Ten Pension Commandments*, 10 J. PENSION PLANNING & COMPLIANCE 405, 405-06 (1984). "ERISA is the very antithesis of simplicity." *Id.* at 406. Congress purposely enacted ERISA in a broad and complex form to fill the void left by the preempted state law which previously dominated the area. See Comment, *Employee Vacation Pay Regulation Under the Employee Retirement Income Security Act of 1974*, 24 SANTA CLARA L. REV. 401, 404-06 (1984).

Since there is nothing in the Act requiring the establishment of a benefit plan, some believe that the complexity of the regulations in ERISA have created a "disincentive" for companies to operate benefit plans. See Grubbs, *The Employee Retirement Income Security Act: The First Decade*, 11 J. PENSION PLANNING & COMPLIANCE 7, 8-9 (1985). This theory has sparked proposals that ERISA again be amended to reduce the burden that complex regulations have imposed upon companies maintaining pension plans. See *id.* at 9; see also Lurie, *supra*, at 406-09 (suggesting ERISA is out of step with Presidential initiatives for government simplification, and proposing reform).

⁴ ERISA § 502(a)(1)(B), 29 U.S.C. § 1132(a)(1)(B) (1982). ERISA's primary goal, employee protection, is advanced by permitting pension beneficiaries and others to bring a federal civil suit to enforce its requirements. See Note, *The Right to Jury Trial in Enforcement Actions under Section 502(a)(1)(B) of ERISA*, 96 HARV. L. REV. 737, 737 (1983).

⁵ See ERISA § 514(a), 29 U.S.C. § 1144(a) (1982). Section 514(a) provides that 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. § 1144(a) (1982). The term "State" is defined as "a State, any political subdivisions thereof, or any agency or instrumentality of either, which purports to regulate . . . the terms and conditions of employee benefit plans covered by this subchapter." *Id.* at § 1144(c)(2). State insurance, banking, and securities laws specifically are not preempted by ERISA. See ERISA § 514(b)(2)(A), 29 U.S.C. § 1144(c)(2)(A) (1982).

The Supreme Court has interpreted the phrase "relate to" in ERISA § 514(a) in its broadest possible sense, viewing ERISA as preempting any state law which has "a connection with or reference to" private pension and welfare plans. See *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 98 (1983); *infra* notes 62-69 and accompanying text. Cf. *Alessi v. Raybestos-Manhattan, Inc.*, 451 U.S. 504, 523 (1981) (Congress' clear intent in section 514 preempting was to make benefit plans an "exclusive federal concern").

It has been suggested that Congress included this sweeping preemptive clause to prevent the great amount of litigation that might be generated by a more narrow provision. See Comment, *supra* note 3, at 408 (citing remarks of Senator Jacob Javits, 120 CONG. REC. 29,942 (1974)). Nevertheless, the courts have been flooded with litigation on the issue of state law preemption. See *id.* at 408 n.46; *infra* notes 63-69 and accompanying text. For an

who control the administration of such plans,⁶ and establishes a cause of action for a breach of these fiduciary duties.⁷ Several courts recently have held that ERISA is applicable and controlling in employee actions to recover compensation due under severance pay benefit plans.⁸

Many companies have established severance benefit plans entitling employees to severance pay if the employment relationship is terminated through no fault of the employee.⁹ Under the modern view, the purpose of severance pay is to allow a terminated employee to find new employment "without substantial losses."¹⁰

excellent analysis of federal preemption in the area of labor law, see Gregory, *Toward Remedying the Concomitant Erosion of the Labor Preemption Doctrine and National Labor Policy*, 27 WM. & MARY L. REV. (to be published in 1986).

⁶ See ERISA § 404(a)(1), 29 U.S.C. § 1104(a)(1) (1982). A person administering a benefit plan is deemed to be a fiduciary with respect to employees participating in the plan if "(i) he exercises any discretionary authority or discretionary control respecting management of such plan . . . (ii) he renders investment advice for a fee . . . with respect to any moneys or other property of such plan . . . or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan." ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A) (1982). This definition has the effect of bringing plan officers, directors and members of the administration of a plan, as well as named trustees (fiduciaries), within the scope of ERISA's fiduciary standards. See Little & Thrailkill, *Fiduciaries Under ERISA: A Narrow Path to Lead*, 30 VAND. L. REV. 1, 4-10 (1977) (many formerly exempt individuals are deemed fiduciaries under ERISA's broad definition).

The fiduciary must "discharge his duties with respect to a plan solely in the interest of the participants . . ." ERISA § 404(a)(1), 29 U.S.C. § 1104(a)(1) (1982). These fiduciaries are required to perform their duties "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use . . ." ERISA § 404(a)(1)(B), 29 U.S.C. § 1104(a)(1)(B) (1982).

⁷ See ERISA § 409, 29 U.S.C. § 1109 (1982).

⁸ See *Holland v. Burlington Indus.*, 772 F.2d 1140, 1145-46 (4th Cir. 1985); *Gilbert v. Burlington Indus.*, 765 F.2d 320, 324-26 (2d Cir. 1985); *Anderson v. Ciba-Geigy Corp.*, 759 F.2d 1518, 1519-20 (11th Cir.), *cert. denied*, 106 S. Ct. 410 (1985); *Barry v. Dymo Graphics Sys.*, 394 Mass. 830, 833-34, 478 N.E.2d 707, 712 (1985).

⁹ See Note, *Severance Pay, Sale of Assets, and the Resolution of Omitted Cases*, 82 COLUM. L. REV. 593, 593 (1982). One third of collective bargaining agreements include severance pay provisions. *Id.* Severance pay has been defined as "[a] payment to a worker upon permanent separation from the company, due to no fault of his own, either in a lump sum or in smaller amounts over a period of time." S. ROBERTS, ROBERTS' DICTIONARY OF INDUSTRIAL RELATIONS 80 (1966). Terminations due to plant or division closings, work slow-downs, or a change in the location of the business operation are common events which trigger severance pay. See Note, *supra*, at 593.

Severance provisions tend to benefit employers as well as their employees. See *Dulaney Foods Inc. v. Ayers*, 220 Va. 502, 504, 260 S.E.2d 196, 199-200 (1979). In fact, a material reason for providing severance pay is "to secure and retain the services of competent employees under difficult and critical labor conditions." *Id.* at 199 (quoting *Hercules Powder Co. v. Brookfield*, 189 Va. 531, 533-34, 53 S.E.2d 804, 808 (1949)).

¹⁰ Gallagher, *Severance Pay: What's the Right Amount?* 46 FIN. EXECUTIVE 32, 34 (Nov. 1978). The Gallagher view of severance pay is that it can be compared to a "bridge" for the

However, at common law, most state courts held that employees who worked for a company that sold its assets were considered "terminated" and deserving of severance pay¹¹ even though the purchasing entity immediately employed the worker to perform the same task, at the same rate of pay, and with the same seniority and benefits.¹² The recent application of ERISA to severance pay claims, however, has completely reversed this situation. Federal courts invariably have held that ERISA preempts state law in actions for the recovery of severance pay after a sale of assets, and

employee who has to relocate and adjust to a new employment position. *See* Gallagher, *supra*, at 34. This theory views the employee's benefit from severance pay as an unemployment-type compensation. *See id.* Thus, one view of the purpose of severance pay "is to provide financial assistance for a short period of time to allow readjustment for salaried employees who are terminated through no fault of their own." *Younger v. Thomas Int'l Corp.*, 275 Ark. 327, 329, 629 S.W.2d 294, 296 (1982) (portion of Warwick Company severance pay policy); *see also* *Pinto v. Zenith Radio Corp.*, 480 F. Supp. 361, 364, (N.D. Ill. 1979) (severance pay policy mandates that employees who find other jobs not entitled to benefit), *aff'd mem.*, 618 F.2d 110 (7th Cir. 1980). However, some courts have disagreed ardently with the allusion to unemployment compensation, viewing severance pay more as remuneration for past services. *See* *Adams v. Jersey Cent. Power & Light Co.*, 21 N.J. 8, 13-14, 120 A.2d 737, 740 (1956); *Owens v. Press Publishing Co.*, 20 N.J. 537, 546, 120 A.2d 442, 446 (1955); *infra* note 11.

¹¹ *See* *Chapin v. Fairchild Camera & Instrument Corp.*, 31 Cal. App. 3d 192, 107 Cal. Rptr. 111 (1973); *Willets v. Emhart Mfg. Co.*, 152 Conn. 487, 208 A.2d 546 (1965); *Fletcher v. Amax, Inc.*, 160 Ga. App. 692, 288 S.E.2d 49 (1981); *Dahl v. Brunswick Corp.*, 277 Md. 471, 356 A.2d 221 (1976); *Anthony v. Jersey Cent. Power & Light Co.*, 51 N.J. Super. 139, 143 A.2d 762 (1958). For additional cases, *see* Note, *supra* note 9, at 595 n.11.

These cases suggest that severance pay is a "liquidated damages provision," benefiting an employee for his employer's breach of the employment relationship, even if the employee is never actually terminated from his physical employment surroundings. *See* Note, *supra* note 9, at 597-98, 605. In contradistinction to the "bridge" theory, *supra* note 10, the liquidated damage approach does not "key eligibility . . . upon continued unemployment. The worker who starts a new job the day after dismissal is as entitled to severance pay as is a worker who remains unemployed." *Id.* This approach compensates an employee for the implicit agreement in his employment relationship with the company that he will continue working so long as his performance is satisfactory. *See id.* at 597. At common law, courts favored the liquidated damage approach over the "bridge" theory. *See, e.g., Dahl v. Brunswick Corp.*, 277 Md. 471, 477, 356 A.2d 221, 227 (1976) (employees selection of "other suitable opening" with purchasing company did not bar severance pay claim); *Adams v. Jersey Cent. Power & Light Co.*, 21 N.J. 8, 10, 120 A.2d 737, 741 (1956) ("loss of employment" not the only means by which employees can collect severance pay); *Dulany Foods, Inc. v. Ayers*, 220 Va. 502, 515, 260 S.E.2d 196, 199 (1979) (unemployment not a prerequisite to severance compensation).

¹² *See* *Mace v. Conde Nast Publications, Inc.*, 155 Conn. 680, 682, 237 A.2d 360, 363 (1967); *Fletcher v. Amax, Inc.*, 160 Ga. App. 692, 701, 288 S.E.2d 49, 51-52 (1981). *But see* *Younger v. Thomas Int., Corp.*, 275 Ark. 327, 329, 629 S.W.2d 294, 296 (1982) (court found it "difficult to envision" a termination where employees were hired by purchaser at same job and salary).

typically have denied claims¹³ despite evidence that the employees have suffered financial injury due to the sale.¹⁴ All employee claimants, whether injured by a sale or not, have had to prove that their employers' decisions to deny severance pay were "arbitrary and capricious" before the courts would overturn such employer decisions.¹⁵

This Note will analyze employee severance pay cases in a sale of assets setting, and will suggest that the financial position of employees *after* the sale should be a determining factor in the adjudication of such claims. The Note will first address state court decisions based upon state law, and will discuss the factual situations, claims, and rationales which often resulted in a victory for employees. The focus will then shift to recent severance pay decisions in which both federal and state courts have agreed that ERISA controls. Standards and methods of ERISA interpretation, which often lead to employer victories, will be discussed. Finally, it will be suggested that courts use a dual standard in adjudicating these claims: if employees are not financially injured by the sale, the "arbitrary and capricious" standard should be applied; if employees lose their seniority or future benefits due to the sale, the strict "fiduciary" standards of ERISA should be used to block employee losses.

¹³ See *Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1149-50 (4th Cir. 1985); *Anderson v. Ciba-Geigy Corp.*, 759 F.2d 1518, 1521-23 (11th Cir.), *cert. denied*, 106 S. Ct. 410 (1985); *Jung v. FMC Corp.*, 755 F.2d 708, 713-15 (9th Cir. 1985); *Sly v. Mallory & Co.*, 712 F.2d 1209, 1213 (7th Cir. 1983); *Pinto v. Zenith Radio Corp.*, 480 F. Supp. 361, 363-64 (N.D. Ill. 1979), *aff'd mem.*, 618 F.2d 110 (7th Cir. 1980). See also *infra* notes 48-61 and accompanying text for ERISA applications in severance pay claims.

¹⁴ See, e.g., *Anderson v. Ciba-Geigy Corp.*, 759 F.2d 1518, 1523 (11th Cir.) (loss of seniority rights and vacation benefits), *cert. denied*, 106 S. Ct. 410 (1985).

This Note will refer to an "injured" or a "financially injured" employee to connote an employee's economic loss due to the sale of his or her company's assets. This loss can take the form of a lower wage after the sale, fewer benefits, or a loss in seniority. Since severance pay plans are generally tied to the seniority of the employee, see Note, *supra* note 9, at 596, a loss of seniority generally means a permanent loss of all accumulated years of severance pay. See *id.*

¹⁵ See *Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1148-49 (4th Cir. 1985); *Anderson v. Ciba-Geigy Corp.*, 759 F.2d 1518, 1520-21 (11th Cir.), *cert. denied*, 106 S. Ct. 410 (1985); *Blau v. Del Monte Corp.*, 748 F.2d 1348, 1352-53 (9th Cir. 1984), *cert. denied*, 106 S. Ct. 183 (1985); *Sly v. Mallory & Co., Inc.*, 712 F.2d 1209, 1211 (7th Cir. 1983); see also *Gilbert v. Burlington Indus., Inc.*, 765 F.2d 320, 329 (2d Cir. 1985) (arbitrary and capricious standard applicable on remand of severance pay claim) (*dicta*). See generally Comment, *The Arbitrary and Capricious Standard Under ERISA: Its Origins and Application*, 23 Duq. L. Rev. 1033 (1985) (arbitrary and capricious standard as applied in ERISA decisions) [hereinafter cited as "Comment, *Arbitrary and Capricious*"].

COMMON LAW TREND:
EMPLOYEE STATE LAW CLAIMS PRIOR TO THE APPLICATION OF
ERISA

Background

Employees often receive handbooks or policy manuals which explain, among other things, their employer's policy toward severance pay.¹⁶ Before the recent adoption of ERISA for the adjudication of claims for severance pay after sales of assets,¹⁷ employee handbooks were almost invariably construed to create binding contractual obligations on the employers, with the result that the employee suits were generally successful.¹⁸ Two defenses were asserted repeatedly by the employers. Employers often claimed that the severance pay provisions contained in the manuals were mere gratuities, lacking consideration from employees, and therefore not binding on the employers.¹⁹ It was also frequently asserted that the sale of a company did not result in a "termination" from employment when the employees were immediately hired by the purchasing company.²⁰ The first argument required the courts to deter-

¹⁶ See Note, *Employee Handbooks and Employment-at-Will Contracts*, 1985 DUKE L.J. 196, 196. Most employee policy manuals contain general employment information about insurance, termination and grievance procedures, and vacation and severance pay policies. *Id.* For examples of severance pay provisions contained in policy manuals, see Note, *supra* note 9, at 593-94 n.4 (eligibility requirements may include moving operation, technological change, closing plant and lack of work).

¹⁷ See Note, *supra* note 9, at 598; see also *supra* note 11 (cases in which employees emerged successful because courts found severance provisions unilaterally binding on employers). For an explanation of the unilateral contract obligation in severance pay claims, see *infra* notes 26 & 29 and accompanying text.

¹⁸ See *infra* notes 48-61 and accompanying text.

¹⁹ See *Dangott v. ASG Indus.*, 558 P.2d 379, 383 (Okla. 1976); *Dulany Foods, Inc. v. Ayers*, 220 Va. 502, 505, 260 S.E.2d 196, 199-201 (1979); see also Note, *Employee Handbooks and Employment-at-Will Contracts*, 1985 DUKE L.J. 196, 200-04 (employer claims that manuals are not contractually binding are typically successful outside severance pay arena). Courts have generally overruled the employers' "gratuity claims" and have held them liable to pay severance. See *Chapin v. Fairchild Camera & Instrument Corp.*, 31 Cal. App. 3d 192, 197, 107 Cal. Rptr. 111, 115-17 (1973); *Gaydos v. White Motor Corp.*, 54 Mich. App. 143, 147-49, 220 N.W.2d 697, 700 (1974); see also *infra* notes 23-30 and accompanying text (analysis of "gratuitous contract" defense in severance pay claims).

²⁰ See, e.g., *Mace v. Conde Nast Publications*, 155 Conn. 680, 684, 237 A.2d 360, 362-63 (1967) (company unsuccessfully claimed employees' immediate acceptance of new job was "novation," not termination); *Adams v. New Jersey Cent. Power & Light Co.*, 21 N.J. 8, 14-15 120 A.2d 737, 740-41 (1956) (company unsuccessfully claimed sale was "mere change of identity"); see also *infra* notes 31-44 and accompanying text (analysis of "no termination" defense in severance pay cases).

mine whether a binding contractual obligation existed;²¹ the second required contract interpretation once such an obligation was found.²²

Severance Provisions as Contractual Obligations

In *Anthony v. Jersey Central Power & Light Co.*,²³ several former employees of Jersey Central brought an action for recovery of severance pay after the company sold its assets to New Jersey Natural Gas Company.²⁴ Prior to the sale, Jersey Central had promulgated and distributed among its employees a "General Rules" pamphlet, which included a provision entitling involuntarily discharged employees to severance pay.²⁵ Although they were reemployed by the purchasing company immediately after the sale, the employees sued to collect severance pay, claiming that the severance pay provision contractually bound Jersey Central to a unilateral obligation.²⁶ In defense, Jersey Central claimed that the provi-

²¹ See *infra* notes 23-30 and accompanying text.

²² See *infra* notes 31-44 and accompanying text.

²³ 51 N.J. Super. 139, 143 A.2d 762 (1958).

²⁴ See *id.* at 141, 143 A.2d at 763. The plaintiff employees in *Anthony* were not members of the labor union which had negotiated with Jersey Central Power & Light for a collective bargaining agreement that included a severance pay provision. See *id.* at 142, 143 A.2d at 764.

A labor agreement can be defined as a third-party beneficiary contract, negotiated and formed between the employer and the union, for the express benefit of the employee-beneficiary. See A. ZACK & R. BLOCH, *LABOR AGREEMENT IN NEGOTIATION AND ARBITRATION* 3-4 (1983). A severance pay agreement can be included in the collective bargaining agreement between the two parties, binding the company to pay severance to the employees according to the terms of the agreement. See *Anthony*, 51 N.J. Super. at 142, 143 A.2d at 763. This Note does not deal with union contracts, or the agreements reached through them. It will focus instead on non-union employees and the effect that severance pay provisions in employment manuals have upon their rights.

²⁵ See *Anthony*, 51 N.J. Super. at 142, 143 A.2d at 763. The General Rules policy stated that the severance pay plan for non-union employees was the same as that set forth in the labor agreement for union employees, one week's pay for each year of service beyond one year. See *id.*

²⁶ See *id.* A unilateral contract is an exception to the "mutuality of obligation" required under bilateral agreements. See J. CALAMARI & J. PERILLO, *CONTRACTS* § 4-15 (3d ed. 1981). In a unilateral contract, the offerees are not required to bind themselves to any form of action to collect upon the offer. See *id.* For example, if severance pay is offered to employees in a policy manual, "[i]t is inconsequential that at no time were the employees requested to or in any way obligated to continue their services." *Id.* The employees are shielded from revocation of the offer if they "accept" the employer's offer by continuing their employment after the promulgation of the manual. See E. FARNSWORTH, *CONTRACTS* § 3.24 (1982); see also *Fletcher v. Amax Inc.*, 160 Ga. App. 692, 693, 288 S.E.2d 49, 51 (1981) (provision for severance pay is offer of contract not void for lack of consideration).

sion was a "mere gratuitous promise" to pay a bonus which was not supported by consideration flowing from either party.²⁷

The New Jersey Appellate Division rejected the employer's defense, holding that the promulgation of a severance pay policy did not contemplate bilateral obligations, but rather formed a unilateral contract.²⁸ Since the employees remained employed with Jersey Central after distribution of the severance policy, Jersey Central's duty to disburse severance pay became a unilateral obligation upon termination.²⁹ The *Anthony* court's rationale has been followed by other courts which have rejected the "mere gratuity" defense.³⁰

"Termination" When Employees Receive Same Employment After Sale

A more difficult theoretical question was raised, however, when companies defended these severance pay suits by contending that a "termination" did not occur when employees received similar positions with purchasing companies.³¹ This issue was addressed in *Willets v. Emhart Manufacturing Co.*³² In *Willets*, the plaintiff employees worked in Emhart's Maxim division, and were entitled to severance compensation if they were "laid off" due to lack of work.³³ Emhart subsequently sold its Maxim division to

²⁷ See *Anthony*, 51 N.J. Super. at 143, 143 A.2d at 764.

²⁸ See *id.*

²⁹ See *id.* *Accord* *Gaydos v. White Motor Corp.*, 54 Mich. App. 143, 148, 220 N.W.2d 697, 700 (1974) (continuation of employment supplied consideration for unilateral contract); *Dulany Foods, Inc. v. Ayers*, 220 Va. 502, 504, 260 S.E.2d 196, 199-201 (1979) (severance pay provision enforceable contract); *Hercules Powder Co. v. Brookfield*, 189 Va. 531, 535, 53 S.E.2d 804, 808-09 (1949) (employees' continued employment for company was consideration for severance pay).

³⁰ See *supra* notes 19 & 29.

³¹ See *Chapin v. Fairchild Camera & Instrument Corp.*, 31 Cal. App. 3d 192, 198, 107 Cal. Rptr. 111, 115 (1973); *Mace v. Conde Nast Publications, Inc.*, 155 Conn. 680, 682, 237 A.2d 360, 363 (1967). In some instances the contract terms themselves have provided different definitions of the meaning of "termination," and therefore may mandate different outcomes. See, e.g., *Younger v. Thomas Int'l Corp.*, 275 Ark. 327, 329, 629 S.W.2d 294, 296 (1982) (by its terms, employees offered equivalent employment upon sale of assets excluded from definition of "termination"); *Linz v. Champion Int'l Corp.*, 675 P.2d 979, 980-81 (Mont. 1984) (same).

³² 152 Conn. 487, 208 A.2d 546 (1965).

³³ See *id.* at 488, 208 A.2d at 547. As part of their employment agreement, the employees in *Willets* were entitled to the benefits included in the company's separation pay agreement contained in a personnel policy statement promulgated two years prior to the sale. *Id.* The agreement provided that the employees "should be eligible to receive the [severance] pay if: (1) the layoff was for an indefinite period; (2) the employee did not voluntarily termi-

American Machine and Foundry Company (A.M.F.), and the plaintiffs elected to work for A.M.F., thus suffering loss of neither compensation nor work time.³⁴ Nevertheless, the employees sued Emhart, claiming that they were laid off and therefore entitled to severance pay.³⁵ In defense, Emhart asserted that because the employees retained their jobs and suffered little or no economic loss, no layoff had occurred and, the employees were not entitled to severance benefits.³⁶

The Connecticut Supreme Court agreed with the employees, holding that the sale was a "layoff" because Emhart could no longer perform its role as employer in the employment relationship.³⁷ The *Willets* court based its interpretation of the employer's obligation solely upon a consideration of the events occurring prior to the sale; the contention that the plaintiffs were never unemployed and suffered little or no economic loss after the sale was deemed irrelevant.³⁸

A different result was reached, however, in the recent case of *Linz v. Champion International Corp.*³⁹ Subsequent to a sale of one of the defendant's divisions, the plaintiff, a former employee of the division sold, rejected an offer of employment with the acquiring company at the same salary.⁴⁰ He then sued his former employer for severance pay, claiming that he had been "terminated"

nate his employment; (3) the employee was not discharged for cause." *Id.*

³⁴ *See id.* Most of the employees working for Emhart suffered no dollar loss, although a few were forced to relocate from Connecticut to Louisiana. *Id.* However, all the employees lost their seniority rights. *See id.*

³⁵ *See id.*

³⁶ *See id.* at 488-89, 208 A.2d at 547.

³⁷ *See id.* "The underlying and determining question is whether these plaintiffs were laid off by the defendant for lack of work." *Id.* The question of whether a business relationship has terminated due to a sale of assets has troubled courts for many years. In *Lovell v. St. Louis Mut. Life Ins. Co.*, 111 U.S. 264 (1884), the Supreme Court held that a life insurance company that sold its assets to another company abandoned any contractual relationship it had with its policy holders; the holders were therefore entitled to consider the policies as terminated and were able to collect the equitable value of the policies. *See Lovell*, 111 U.S. at 274-76. The *Willets* court applied analogous reasoning in holding that Emhart's voluntary act made it impossible for the employees to continue a contractual relationship with the company. *See Willets*, 152 Conn. at 488, 208 A.2d at 548.

³⁸ *See Willets*, 152 Conn. at 489, 208 A.2d at 548. Emhart asserted that the important factors in determining whether its former employees were entitled to severance pay were the events occurring after the sale of assets. *See id.* The court disagreed, and stated that severance pay "concerns the past, not the future, and once it is earned, it becomes payable no matter what may thereafter happen." *Id.*

³⁹ 675 P.2d 979 (Mont. 1984).

⁴⁰ *See id.* at 979-80.

and was therefore entitled to severance benefits in accord with Champion's stated policy.⁴¹ The Montana Supreme Court held, however, that this was *not* a termination triggering severance pay, since the plaintiff could have worked in substantially the same capacity for the same salary.⁴² Thus, in contrast to the *Willets* court, the *Linz* court focused its analysis on the financial position of the employee after the merger.⁴³ It is suggested that the approach adopted by the *Linz* court is a more rational and equitable method of adjudicating these claims because the possibility of double recovery by the employee is minimized.⁴⁴ However, the present im-

⁴¹ See *id.* at 980. The plaintiff in *Linz* was a data processing employee of the Hoerner Waldorf Corporation, which merged with Champion International Corporation in 1977. See *id.* at 979. Champion adopted a severance pay policy in 1977 for employees terminated due to the merger, which stated: "[s]alaried employees of Hoerner Waldorf and other units of Champion International whose employment is terminated as a result of the merger shall be entitled to severance pay based upon length of service." *Id.* at 979-80.

⁴² See *id.* at 980-81. The *Linz* court adopted a literal definition of "termination" of employment, holding that "termination" means "to put an end to; to make to cease; to end." See *id.* at 981 (quoting BLACK'S LAW DICTIONARY 1319 (5th ed. 1979)). Champion offered the employee a comparable position in the same city; thus the court did not find that the employee's employment was terminated. *Id.* Accord *Livernois v. Warner-Lambert Co.*, 723 F.2d 1148, 1156 (4th Cir. 1983) (no employee termination if purchasing company supplies same job); *Younger v. Thomas Int'l Corp.*, 275 Ark. 327, 329, 629 S.W.2d 294, 296 (1982) (no employee termination when "the only change of any significance was the name of their employer").

⁴³ Compare *Linz*, 675 P.2d at 980-81 (financial position of employee after merger crucial) with *Willets*, 152 Conn. at 488, 208 A.2d at 548 (events subsequent to buy-out irrelevant).

⁴⁴ In recent cases, courts have tended to divert from narrow holdings like the *Willets* decision, which analyzed only events occurring prior to the sale. In cases falling under ERISA, with almost identical fact situations as the *Willets* or *Anthony* decisions, see *supra* notes 23-26 & 32-34 and accompanying text, courts have taken into account events occurring after the sale in determining whether a termination had occurred. See, e.g., *Jung v. FMC Corp.*, 755 F.2d 708, 714 (9th Cir. 1985) (award of severance pay to employees retaining previous position and benefits would result in windfall); *Pinto v. Zenith Radio Corp.*, 480 F. Supp. 361, 364 (N.D. Ill. 1979) (subsequent events become important because of contract terms, and employees immediately rehired held not entitled to severance pay), *aff'd*, 618 F.2d 110 (7th Cir. 1980). It is suggested that to ascertain whether severance pay is "earned," one must ascertain whether the employee has become terminated. This can be done only by taking into account events which occur after the sale of assets.

It is also suggested that the *Linz* court adjudicated the matter before it in a more equitable fashion than did the *Willets* court. The *Willets* opinion seems ultimately correct in awarding severance pay to the former Emhart employees because they suffered economic loss due to the sale. See *supra* note 34. However, it is submitted that the *Willets* analysis is weak because it adjudicated the case solely on the basis of events prior to the sale, without viewing the employees future economic position after the sale. Analysis such as this may lead to employee double recovery of severance pay. Cf. *Jung v. FMC Corp.*, 755 F.2d 708, 714 (9th Cir. 1985) (double recovery should not be favored).

portance of the common law contractual interpretations has diminished due to the sweeping impact of ERISA upon the severance pay field.

RECENT TREND:
ERISA COVERAGE OF SEVERANCE PAY CLAIMS

Recently, corporations engaged in mergers, acquisitions, and sale of assets have found it necessary to cautiously weigh the impact of changes in ownership upon the employee benefit plans of the entity being acquired.⁴⁵ Before the enactment of ERISA, such considerations were typically given only a cursory review at the last moment of negotiations.⁴⁶ There is presently an understanding in the business community, however, that the status of a seller's benefit plans can affect the price of the sale, the method of acquisition and the future financial development of the acquired entity.⁴⁷ It is submitted that the very recent federal decisions, holding that ERISA is controlling and applicable to the severance benefit field, are a part of this trend, and have dramatically changed this area of the law.

Applicability

Attempting to preserve favorable common law trends and avoid ERISA's sweeping preemption of state law,⁴⁸ employees have unsuccessfully argued in recent cases that ERISA's definition of an "employee welfare benefit plan" does not include unfunded sever-

⁴⁵ See generally Reichler, *Handling Significant Benefit Plans in Mergers & Acquisitions*, 2 Bus. Acquisitions 831, 831-70 (2d ed. 1981).

⁴⁶ See *id.* at 831.

⁴⁷ See *id.* at 831-35. Although not typically included in the past, most corporate acquisitions now include provisions for the purchasing company to assume the selling company's employee benefit plans. See Grienerberger & Wright, *Securities Law Aspect of the Acquisition of a Publicly[sic] Held Company*, 1 Bus. Acquisitions 568, 578 (2d ed. 1981). In some cases the plans of the acquired company terminate and fold into the purchasing company's benefit plans; in others, the employer's plans are maintained as originally provided. See *id.* at 578.

⁴⁸ See *supra* note 5 and accompanying text. Employees have continued to bring severance pay actions in state courts under state law claims even though ERISA has been held to preempt this field. See *Barry v. Dymo Graphic Sys.*, 394 Mass. 830, 832, 478 N.E.2d 707, 709 (1985). In *Barry*, the employees won a severance pay claim in a lower Massachusetts court on state law grounds, but on appeal to the Supreme Judicial Court of the state, the company successfully raised the preemption issue and the decision was reversed. See *id.* at 709, 712.

ance pay provisions.⁴⁹ Employees have theorized that since severance pay is not mentioned specifically as a "welfare plan" in the statute, it should not be covered by ERISA.⁵⁰ This argument, however, has been unanimously rejected by recent federal and state court decisions.⁵¹

Section 3(1)(B)⁵² indicates that in addition to the express benefits listed, "any benefit described" in section 186(c) of the Labor Management Relations Act (LMRA)⁵³ will also be considered an

⁴⁹ See *Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1145-46 (4th Cir. 1985); *Gilbert v. Burlington Indus.*, 765 F.2d 320, 326 (2d Cir. 1985); *Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1502 (9th Cir. 1985).

A funded pension plan is defined as one maintained either in part or wholly through employee contributions. See ERISA §§ 301 & 302, 29 U.S.C. §§ 1081 & 1082 (1982) (coverage and minimum funding standards for pension plans). Provided certain requirements are met, such a pension plan becomes a vested interest of the employee who contributed the funds. See ERISA §§ 201 & 203, 29 U.S.C. §§ 1051 & 1053 (1982) (vesting coverage and minimum vesting standards). To the extent that employees do not contribute to the benefit plans, the plans are deemed to be unfunded. "Employee welfare benefit plans," which are expressly exempted from ERISA funding requirements, see ERISA § 301(a)(1), 29 U.S.C. § 1081(a)(1) (1982), do not vest in the employee, see ERISA § 201, 29 U.S.C. § 1051 (1982).

Employees have argued that ERISA was not meant to deal with severance pay because severance pay is typically not funded by employees, and benefits are typically paid from a company's general assets. See *Gilbert v. Burlington Indus.*, 765 F.2d 320, 325 (2d Cir. 1985). Ironically, in older severance pay cases, the employees encouraged the application of ERISA, apparently to take advantage of the strict "fiduciary duty" standard imposed on their employers. See *Petrella v. NL Indus.*, 529 F. Supp. 1357, 1361 (D.N.J. 1982). However, with the federal courts' application of the less stringent "arbitrary and capricious" standard, employees more recently have argued that the "pro-employee" statute does not apply. See *Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1145-46 (4th Cir. 1985); *Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1502 (9th Cir. 1985); see also *infra* notes 112-120 and accompanying text (suggesting that present inflexible ERISA standards must be modified to bring equity to severance field).

⁵⁰ See *Gilbert v. Burlington Indus.*, 765 F.2d 320, 325 (2d Cir. 1985). ERISA does not specifically mention severance pay as an included "welfare plan." ERISA § 3(1)(A), 29 U.S.C. § 1002(1)(A) (1982); *Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1145-46 (4th Cir. 1985) (employees assert severance plan was not ERISA "welfare plan").

⁵¹ See, e.g., *Holland*, 772 F.2d at 1144 (4th Cir. 1985); *Gilbert*, 765 F.2d at 325 (2d Cir. 1985); *Petrella v. NL Indus.*, 529 F. Supp. 1357, 1361-62 (D.N.J. 1982); *Barry v. Dymo Graphic Sys., Inc.*, 394 Mass. 830, 835, 478 N.E.2d 707, 712 (1985). "Subsection (A) [ERISA § 3(1)(A), 29 U.S.C. § 1002(1)(A) (1982)] refers to 'unemployment' benefits. Severance pay, which in general is intended to tide an employee over while seeking a new job, certainly could be considered an 'unemployment' benefit . . . It appears, therefore that . . . Congress intended the term 'welfare plan' to include a plan for severance benefits." *Petrella*, 529 F. Supp. at 1361-62.

⁵² ERISA § 3(1)(B), 29 U.S.C. § 1002(1)(B) (1982).

⁵³ LMRA § 302(c), 29 U.S.C. § 186(c) (1982). This Note will refer to section 302 of the LMRA as "section 186(c)" as it appears in the text of ERISA § 3(1)(B), 29 U.S.C. 1002(1)(B) (1982).

employee welfare benefit plan for purposes of ERISA.⁵⁴ Section 186(c) of the LMRA concerns money paid to funds for "pooled vacation, holiday, severance or similar benefits."⁵⁵ According to the Department of Labor, the reason section 186(c) was mentioned in ERISA was to include severance pay benefits within the definition of an employee welfare benefit plan.⁵⁶ Recent federal decisions have agreed with this interpretation, holding that unfunded severance pay policies are employee welfare benefit plans within the meaning of section three of ERISA.⁵⁷ It has also been noted that Congress effectively sanctioned the Department of Labor's view in an amendment to section 3(2)(B).⁵⁸

⁵⁴ See ERISA § 3(1)(B), 29 U.S.C. § 1002(1)(B) (1982). ERISA defines a benefit plan as either an "employee pension benefit plan" or an "employee welfare benefit plan." See ERISA § 3(1), (2), 29 U.S.C. § 1002(1)-(2) (1982). Under the "welfare benefit" section, ERISA § 3(1), 29 U.S.C. 1002(1) (1982), Congress expanded the enumerated benefits in section (A) by including "any benefit described in section 186(c)" of the LMRA in section (B). See ERISA § 3(1), 29 U.S.C. 1002(1) (1982). For a review of ERISA's coverage of benefit plans, see Goodman & Stone, *Exempt Compensation Arrangements Under ERISA*, 28 CATH. U.L. REV. 445 (1979).

⁵⁵ See LMRA § 302(c)(6), 29 U.S.C. § 186(c)(6) (1982). Section 186 of the LMRA prohibits employers from giving gifts or loans of money or property to labor advisors or representatives of employees. See *id.*; see also *Music v. Western Conference of Teamsters Pension Trust Fund*, 712 F.2d 413, 416 (9th Cir. 1983) (gift-giving from employees to trustees prohibited). Although Section 186(c) refers only to *pooled* severance benefits, the word "pooled" has been construed as having no effect in limiting either the broad, ordinary meaning of severance pay or its coverage under ERISA. See *Gilbert v. Burlington Indus.*, 765 F.2d 320, 325 (2d Cir. 1985).

⁵⁶ See 29 C.F.R. § 2510.3-1(a)(3) (1985). The United States Department of Labor is empowered to enforce ERISA. See ERISA § 502(a)(2), (a)(4)-(6), 29 U.S.C. 1132(a)(2), (a)(4)-(6) (1982). The regulation in question is an interpretation by the Department of Labor that unfunded severance pay benefit plans are within the definition of an ERISA "welfare benefit plan." See 29 C.F.R. § 2510.3-1(a)(3) (1985).

⁵⁷ See *Gilbert v. Burlington Indus.*, 765 F.2d 320, 325 (2d Cir. 1985); *Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1502 (9th Cir. 1985); *Blau v. Del Monte Corp.*, 748 F.2d 1348, 1352 (9th Cir. 1985), *cert. denied*, 106 S. Ct. 183 (1985). In *Gilbert*, the court recognized that agency interpretations of federal statutes are entitled to deference. See *Gilbert*, 765 F.2d at 325. Reviewing ERISA's legislative history, in particular Senator Javits' proposed amendment, see S. REP. NO. 127, 93rd Cong., 2d Sess. 3, *reprinted in* 1974 U.S. CODE CONG. & AD. NEWS 4639, 4838, 4851, the court determined that the Department of Labor's construction of section 3(1)(B) of ERISA was reasonable, and therefore, severance pay should be included within that definition. See *Gilbert*, 765 F.2d at 326. *Accord* *Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1502 (9th Cir. 1985); *Donovan v. Dillingham*, 688 F.2d 1367, 1371 (11th Cir. 1982); *Pinto v. Zenith Radio Corp.*, 480 F. Supp. 361, 363 (N.D. Ill. 1979), *aff'd mem.*, 618 F.2d 110 (7th Cir. 1980).

⁵⁸ See *Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1145 (4th Cir. 1985) ("This amendment . . . sanctioned these regulations and provided that severance pay arrangements . . . would be subject to [ERISA]."). In 1980, after the Department of Labor promulgated its regulation stating that severance pay was to be included in ERISA, Congress amended

Alternatively, employees have asserted that unfunded severance plans are really payroll practices, and therefore should not be considered welfare plans within the scope of ERISA.⁵⁹ However, severance plans require an extra disbursement of funds beyond regular payroll disbursements;⁶⁰ thus ERISA should apply, because a principle concern of the statute is the possibility that employers may default on potentially large blocks of benefit claims.⁶¹ It is suggested, therefore, that no conflict exists with respect to the proposition that ERISA is applicable in severance pay actions after a sale of assets.

Preemption

The enactment of ERISA was intended to make the control of private pension and welfare benefit plans an exclusively federal matter.⁶² Toward this end, section 514(a) provides that ERISA "shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan."⁶³ Although courts

ERISA § 3(2)(B), 29 U.S.C. § 1002(2)(B) (1982). This section reads: "The Secretary may by regulation prescribe rules consistent with the standards and purposes of this act providing one or more exempt categories under which -

(i) severance pay arrangements . . . shall, for purposes of this title, be treated as welfare plans rather than pension plans." ERISA § 3(2)(B), 29 U.S.C. § 1002(2)(B) (1982). It is suggested that this amendment casts aside any doubts as to whether severance pay is an "employee welfare benefit plan" covered by the statute. *See Holland*, 772 F.2d at 1145.

⁵⁹ *See, e.g., Holland*, 772 F.2d at 1145; *Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1502 (9th Cir. 1985). In *Scott*, the employees argued that severance pay should be included in the Department of Labor's list of "payroll practices," which includes jury duty, medical leaves and holidays. *See Scott*, 754 F.2d at 1502; *see also* 29 C.F.R. § 2510.3-1(b)(2)-(3) (1985).

⁶⁰ *See, e.g., Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1503 (9th Cir. 1985). The *Scott* court suggested that severance pay logically should be distinguished from payroll practices. *See id.* While the practices described in the regulations require ordinary disbursements of funds and wages, these payments typically take place during the continuing term of employment. *Id.* at 1503. "Severance pay, in contrast, requires an extra disbursement of funds . . . at or after the termination of employment." *See Scott*, 754 F.2d at 1503.

⁶¹ *See Scott*, 754 F.2d at 1503. The *Scott* court asserted that because of the "extra disbursement" severance pay requires, the danger that an employer may default on severance pay obligations is greater than the danger of his default on medical or vacation pay. *See id.*

⁶² *See House Report, supra* note 2, at 4642-43 (ERISA was established as a federal remedy for inadequate state law in pension benefit arena).

⁶³ ERISA § 514(a), 29 U.S.C. § 1144(a) (1982). The explicit preemption of state law serves the purpose of creating federal control over private pension benefit plans in America. *See Alessi v. Raybestos-Manhattan, Inc.*, 451 U.S. 504, 523 (1981); *supra* note 5; *see also* Comment, *supra* note 3, at 408. *But cf. Metropolitan Life Ins. Co., v. Massachusetts*, 105 S. Ct. 2380, 2399, (1985) (insurance contracts purchased for plans under ERISA come within statutory exception to preemption).

have differed in defining the parameters of the rather amorphous phrase "relate to,"⁶⁴ the preemptive provision was recently given an expansive interpretation by the Supreme Court in *Shaw v. Delta Airlines, Inc.*⁶⁵

In *Shaw*, a group of Delta Airlines employees brought an action against the company for violations of state law, claiming discrimination in the administration of Delta's employee benefit plans.⁶⁶ Rejecting the notion that state law is preempted by ERISA only if it is "specifically designed to affect employee benefit plans,"⁶⁷ the Court held that the words "relate to" in section

The Supremacy Clause of the United States Constitution mandates that federal law shall preempt or supersede all conflicting state law. See U.S. CONST. art. VI, cl. 2. Thus, the federal preemption of state law finds its roots in the Supremacy Clause. See generally J. NOWACK, R. ROTUNDA & J. YOUNG, CONSTITUTIONAL LAW 292-95 (2d ed. 1983); Gregory, *supra* note 5; Note, *A Framework for Preemption Analysis*, 88 YALE L.J. 363 (1978).

⁶⁴ See Comment, *ERISA Preemption of State Vacation Pay Laws: California Hospital Association v. Henning*, 16 LOY. U. CHI. L.J. 387, 397 (1985) [hereinafter cited as *ERISA Preemption*]. Analyses of preemption claims have generally focused upon one of three issues: (1) whether the state law conflicts with the purposes of ERISA; (2) whether the state law's purpose is directed at employee benefit plans; or (3) whether the effect of the state law is so minimal as to render it exempt from preemption. See *id.* For analyses of ERISA preemption, see Caples, *ERISA, Preemption, and California Community Property Law*, 22 SANTA CLARA L. REV. 33 (1982); Hutchinson & Ifshin, *supra* note 2; Note, *ERISA Preemption of State Law: The Meaning of "Relate To" in Section 514*, 58 WASH. U.L.Q. 143 (1980).

The broad ERISA preemption, however, does not contemplate a concomitant lack of judicial power to formulate ERISA common law. See Ray & Halpern, *The Common Law of ERISA*, 21 TRIAL 20 (1985):

Labor lawyers have long been familiar with the power . . . of the federal judiciary to formulate a substantive federal common law of labor management relations to supplement enactments of Congress It is not well known, however, that in enacting . . . ERISA, the United States Congress directed courts to play the same role in developing the federal regulatory scheme for employee benefits.

Id. at 20 (citations omitted). See *infra* notes 76-81 and accompanying text for additional analysis of judicial power to create ERISA common law.

⁶⁵ 463 U.S. 85 (1983).

⁶⁶ See *id.* at 92. The *Shaw* case involved an action brought by Delta employees under the New York Human Rights Law, the New York Disability Law and the New York Worker's Compensation Law. See *id.* at 88-89. The Disability Law issue was dealt with separately, and was found not to be preempted by ERISA because of an express exemption of certain disability plans under ERISA section 4(b)(3), 29 U.S.C. § 1003(b)(3) (1982). See *id.* at 106-08 (plans which Disability Law regulate are exempt from ERISA under section 4(b)).

The employees claimed that the Delta plan discriminated against them on the basis of pregnancy. See *Shaw*, 463 U.S. at 88. Prior to *Shaw*, sex discrimination and fair employment employee actions were generally not held to be preempted by ERISA because, among other reasons, they "failed to conflict with any of ERISA's provisions." *ERISA Preemption*, *supra* note 64, at 402 (citation omitted).

⁶⁷ See *Shaw*, 463 U.S. at 98.

514(a) must be used in their broad sense.⁶⁸ Thus, since *Shaw*, state law claims have been preempted by ERISA if they have a "connection with or reference to" private pension plans.⁶⁹

In the context of severance claims after a sale of the assets of a company, federal courts have consistently held that state law claims brought by employees are preempted by ERISA.⁷⁰ Two ba-

⁶⁸ See *id.* Justice Blackmun, writing for a unanimous Court, noted that a narrow interpretation of the words "relate to" would ignore the intent of the statute. See *id.* The Court attempted to define the general parameters of the phrase, stating that "[A] law 'relates to' an employee benefit plan, in the normal sense of the phrase, if it has a connection with or reference to such a plan" (citing BLACKS LAW DICTIONARY 1158 (5th ed. 1979)). *Id.* at 97. As support, the Supreme Court referred to the more narrow preemptive clause suggested in the original version of ERISA, that limited preemption solely to state laws "relat[ing] to the reporting and disclosure responsibilities, and fiduciary responsibilities, of persons acting on behalf of any employee benefit plan . . ." *Id.* at 98 n.18 (quoting H.R. REP. NO. 2, 93d Cong., 2d Sess., § 514(a) (1974), reprinted in 3 LEGISLATIVE HISTORY OF THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974 4057-58) (1976). For additional selected ERISA legislative history relating to § 514(a), see *ERISA Preemption*, *supra* note 64 at 403-04 n.122-24.

⁶⁹ See *Shaw*, 463 U.S. at 96-97; Kilberg & Inman, *Preemption of State Law Under ERISA: Drawing the Line Between Laws That Do and Laws That Do Not Relate To Employee Benefit Plans*, 19 FORUM 162, 167-68 (1983); see also *Gilbert v. Burlington Indus.*, 765 F.2d 320, 326-27 (2d Cir. 1985) (*Shaw* rejects narrow preemption). *But see Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1502, 1504-06 (9th Cir. 1985) (retroactive/prospective dichotomy preemption issue).

According to the *Scott* court, the employees' state law claim for the recovery of future benefits due was not preempted by ERISA. See *Scott*, 754 F.2d at 1505-06. The employees' claim alleged "the violation of Gulf's duties as a past employer. . . . The claim does not raise any issues concerning the matters regulated by ERISA . . ." *Id.* It is suggested, however, that the broad scope of the ERISA preemption, broadened by *Shaw*, also encompasses tort claims for prospective loss filed against the fiduciaries of an employee's welfare fund, *i.e.*, the executives directing Gulf's severance pay policy. The rationale of the *Scott* court was that the employees' claim "does not raise any issues concerning the matters regulated by ERISA . . ." *Id.* at 1505. However, the Supreme Court in *Shaw* explicitly rejected this type of anti-preemption argument, explaining that ERISA was amended from an Act that preempted only certain state laws "relat[ing] to the reporting and disclosure responsibilities" of the trustees, *Shaw*, 463 U.S. at 98 n.18, to the present form that preempts any state law which "relate[s] to any employee benefit plan . . ." ERISA § 514(a), 29 U.S.C. 1144(a) (1982) (emphasis added). Thus, it is suggested that the claim presented in *Scott* should not have bypassed ERISA's broad preemption. It is also suggested that the strong preemption message gleaned from the *Shaw* Court may be a start toward stemming the erosion of federal labor preemption, which yields hope for a return to a strong federal labor policy. See Gregory, *supra* note 5 (advocating remedy of weak labor policy with return of strong federal preemption).

⁷⁰ See *Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1147 (4th Cir. 1985); *Gilbert v. Burlington Indus.*, 765 F.2d 320, 327 (2d Cir. 1985); *Dependahl v. Falstaff Brewing Corp.*, 653 F.2d 1208, 1215 (8th Cir.), *cert. denied*, 454 U.S. 968 (1981). *But see Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1506 (9th Cir. 1985) (employees' claim not preempted insofar as it alleges loss of future severance benefits possibly accumulated during employment with new company).

ses have been suggested as necessitating such preemption: a statutory argument under section 514(a),⁷¹ and a general preemption argument based on the assertion that ERISA is a complete and comprehensive regulatory statute.⁷² The former was definitively supported by *Shaw*.⁷³ It has been suggested, however, that the latter argument cannot stand.⁷⁴

Although Congress prescribed a multitude of regulatory terms in ERISA,⁷⁵ the statute's broad scope does not in itself suggest that it preempts all common law developed in the field of labor.⁷⁶

In *Dependahl v. Falstaff Brewing Corp.*, 653 F.2d 1208 (8th Cir.), *cert. denied*, 454 U.S. 968 (1981), the Court of Appeals for the Eighth Circuit held that ERISA preempted employees' state law claims of tortious interference with contract after a sale of corporate assets. *See id.* at 1214-16. Denying the employees' state law claims for the recovery of severance pay, the *Dependahl* court ruled that the broad scope of ERISA's substantive provisions, combined with its specific preemption in section 514, necessitated a finding that the state claims were preempted. *See id.* at 1215. Although in *Dependahl* the employees ultimately emerged victorious, *see id.* at 1219-20, when ERISA blocks employee state law claims, the employers typically win. *See Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1149-50 (4th Cir. 1985); *Anderson v. Ciba Geigy Corp.*, 759 F.2d 1518, 1521-23 (11th Cir.), *cert. denied*, 106 S. Ct. 410 (1985); *Jung v. FMC Corp.*, 755 F.2d 708, 713-15 (9th Cir. 1985); *Sly v. Mallory & Co.*, 712 F.2d 1209, 1213 (7th Cir. 1983). A 1985 Massachusetts state court decision has also echoed the federal pattern, holding that ERISA preempts Massachusetts law in severance pay claims after a sale of assets. *See Barry v. Dymo Graphic Sys., Inc.*, 394 Mass. 830, 834, 478 N.E.2d 707, 711-12 (1985).

⁷¹ 29 U.S.C. § 1144(a) (1982). *See Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 98-100 (1983); *Dependahl v. Falstaff Brewing Corp.*, 653 F.2d 1208, 1215 (8th Cir.), *cert. denied*, 454 U.S. 968 (1981). Along with the broad scope of ERISA's regulations, the court noted that "the explicit statement of federal preemption in section 1144 [ERISA § 514], leads us to conclude that Congress intended to 'occupy the field' of employee benefit plans." *Id.* *Accord Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1147 (4th Cir. 1985) (Congress intended to "sweep" away related state law with section 514(a) preemption); *Gilbert v. Burlington Indus.*, 765 F.2d 320, 326 (2d Cir. 1985) (same).

⁷² *See Dependahl*, 653 F.2d at 1215. "[T]he broad scope of the substantive provisions of ERISA . . . lead us to conclude . . . that Congress legislated an ouster of all state laws relating to employee benefit plans . . ." *Id.*

⁷³ *See Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 96-100 (1983) ("The breadth of § 514(a)'s pre-emptive reach is apparent from that section's language.")

⁷⁴ *See Caples, supra* note 64, at 55-56. The author suggests that although ERISA is extremely comprehensive, no statute can be comprehensive enough to preempt every law even tangentially affecting employee benefit plans. *See id.*; *infra* notes 76-81 and accompanying text.

⁷⁵ *See ERISA*, 29 U.S.C. § 101 *et seq.* (1982). ERISA sets out regulatory provisions for reporting and disclosure, *see ERISA* §§ 101-110, 29 U.S.C. §§ 1021-1031 (1982), participation and vesting, *see ERISA* §§ 201-211, 29 U.S.C. §§ 1051-1061 (1982), funding, *see ERISA* §§ 301-306, 29 U.S.C. §§ 1081-1086 (1982), fiduciary responsibility, *see ERISA* §§ 401-414, 29 U.S.C. §§ 1101-1145 (1982), and administration and enforcement, *see ERISA* §§ 501-515, 29 U.S.C. §§ 1201-1242 (1982). *See generally* Grubbs, *supra* note 3 (description of ERISA sections); Gertner, *ERISA in Retrospect*, 10 J. PENSION PLANNING & COMPLIANCE 275 (1984) (same).

⁷⁶ *See Caples, supra* note 64, at 55-56 (breadth of ERISA's scope does not in itself

To the contrary, Congress realized that no matter how detailed ERISA was, it could not be so specific as to fill completely an area of law formerly dominated by state regulation and common law.⁷⁷ Therefore, Congress empowered the federal courts to develop a body of federal common law governing employee benefit plans to fill the void caused by the preemption of state law.⁷⁸ Standards that have been developed under state and federal labor adjudications may be used to develop this common law into ERISA interpretations,⁷⁹ but only to the extent that these standards are consistent with the pro-employee policy objectives of ERISA.⁸⁰ It is suggested that in recent severance pay cases, however, federal courts have not made use of ERISA's flexibility to create an equitable body of federal common law; they have merely mimicked one another without weighing the validity of applying the same rigid standards to each case and without considering the financial injury suffered by employees after the sale in the ultimate determination.⁸¹

support preemption argument).

⁷⁷ See 120 CONG. REC. 29942 (1974), reprinted in 3 LEGISLATIVE HISTORY OF THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974 (1976) (remarks of Senator Javits suggesting Congress intended a body of common law to be fashioned from ERISA). See also *Menhorn v. Firestone Tire & Rubber Co.*, 738 F.2d 1496, 1499 (9th Cir. 1984) (Congress empowered courts to develop, in light of reason and experience, a body of federal common law governing employee benefit plans). Accord *Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1502 (9th Cir. 1985); *Hayden v. Texas-U.S. Chem. Co.*, 681 F.2d 1053, 1057 (5th Cir. 1982).

⁷⁸ See *Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1502 (9th Cir. 1985); *Menhorn v. Firestone Tire & Rubber Co.*, 738 F.2d 1496, 1499 (11th Cir. 1984); *Thorton v. Evans*, 692 F.2d 1064, 1079 (7th Cir. 1982); *Ray & Halpern*, *supra* note 64, at 21-22; *ERISA Preemption*, *supra* note 64, at 398.

⁷⁹ See *Ray & Halpern*, *supra* note 64, at 22. Section 3(A) of ERISA, 29 U.S.C. § 1002(A) (1982), makes reference to section 186 of the LMRA. See *supra* note 2 for text of ERISA § 3(A). It has been suggested that the reference to the LMRA in ERISA solidifies the notion that Congress intended to have the judiciary integrate other federal labor policy into ERISA. See *Menhorn v. Firestone Tire & Rubber Co.*, 738 F.2d 1496, 1499-1500 (9th Cir. 1984).

⁸⁰ Cf. ERISA § 2(b), 29 U.S.C. § 1001(b) (1982) ("It is hereby declared to be the policy of this chapter to protect . . . the interests of participants in employee benefit plans"); *supra* notes 2 & 4 and accompanying text. By enacting ERISA, Congress gave the courts great power to modify old standards so that they would be consistent with ERISA's pro-employee policies. See *Ray & Halpern*, *supra* note 64, at 22. Therefore, although ERISA preempts state law that "relate[s] to" pension and welfare benefit plans, see *supra* notes 69-70, federal courts are free to extrapolate relevant state law that is consistent with ERISA's policies, and develop it into ERISA federal common law. See *Ray & Halpern*, *supra* note 64, at 22.

⁸¹ See *supra* note 8. It is suggested that upon analyzing severance pay cases in which ERISA has been applied, one finds differing degrees of employee injury, yet surprisingly similar outcomes. There seems to be strong reliance between the courts upon each other's decisions in applying methods of ERISA adjudication especially in relation to the arbitrary and

ERISA STANDARDS

ERISA defines a fiduciary as a person who possesses any control, responsibility or authority with regard to the operation or management of employee benefit plans.⁸² The fiduciaries must perform their function with the skill that a prudent man would use when acting in the same capacity and circumstance.⁸³ Generally speaking, there are two standards by which to measure the propriety of the fiduciary's actions: the duty of loyalty, set out in ERISA,⁸⁴ and the arbitrary and capricious standard, developed at common law.⁸⁵

ERISA's Duty of Fiduciary Loyalty Standard

ERISA imposes a duty of fiduciary loyalty upon the those who

capricious standard. *See e.g.*, *Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1149 (4th Cir. 1985) ("no reason to vary the [arbitrary and capricious] standard"); *see also* *Anderson v. Ciba-Geigy Corp.*, 759 F.2d 1518, 1521 (11th Cir.) (no authority for proposition that ERISA requires something other than arbitrary and capricious standard of review), *cert. denied*, 106 S. Ct. 410 (1985). In other decisions, however, while still relying upon each other in selecting the arbitrary and capricious standard, courts have hinted that the arbitrary and capricious standard may not be the only standard that applies. *See, e.g.*, *Jung v. FMC Corp.*, 755 F.2d 708, 711 (9th Cir. 1985) ("[w]hatever may be the appropriate standard of review in cases like *Struble*, [723 F.2d 325 (3d Cir. 1984)] the arbitrary and capricious standard seems adequate for the purposes of ERISA in situations before us."); *Blau v. Del Monte Corp.*, 748 F.2d 1348, 1353 (9th Cir. 1984) ("[w]e do not decide that this [arbitrary and capricious standard] is the only applicable standard of review . . ."), *cert. denied*, 106 S. Ct. 183 (1985). *But cf.* *Struble v. New Jersey Brewery Employees' Welfare Trust Fund*, 732 F.2d 325, 332-34 (3d Cir. 1984) (in non-sale of assets case, court applies ERISA fiduciary standard of care, rather than arbitrary and capricious standard, to trustee action).

⁸² *See* ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A) (1982). Fiduciary obligations are imposed upon any person to the extent that "(i) he exercises any discretionary authority or discretionary control respecting management of such [employee benefit] plan . . . (ii) he renders investment advice for a fee . . . or (iii) he has any authority or discretionary responsibility in the administration of such plan." *Id.*

⁸³ *See* ERISA § 404(a)(1)(B), 29 U.S.C. § 1104(a)(1)(B) (1982). Section 404 provides:

(A) *Prudent man standard of care* (1) . . . a fiduciary shall discharge his duties with respect to a plan . . .

(B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims;

Id.

⁸⁴ *See* ERISA § 404(a)(1), 29 U.S.C. § 1104(a)(1) (1982); *infra* notes 86-89 and accompanying text. *See also supra* note 6 (selected text).

⁸⁵ *See* Comment, *Arbitrary and Capricious*, *supra* note 15, at 1037-38 (arbitrary and capricious standard evolved from state common law standards); *infra* notes 92-95 and accompanying text.

ERISA's Duty of Fiduciary Loyalty Standard

ERISA imposes a duty of fiduciary loyalty upon the those who "control" employee benefit plans.⁸⁶ Thus, the duty of fiduciary loyalty may be imputed to a corporate executive even though he or she may not be officially labeled a trustee or fiduciary.⁸⁷ Section 404(a)⁸⁸ mandates that a fiduciary "discharge his duties with respect to [the] plan solely in the interests of the participants," and act exclusively toward providing benefits with minimum administrative expense.⁸⁹ This strict fiduciary standard has generally been applied when employees challenge the actions of their fiduciary/trustees, alleging that the trustees have sacrificed the employees' valid interests principally to advance the interests of third parties.⁹⁰

Judicially Applied Arbitrary and Capricious Standard

Although seemingly required to do so by ERISA, courts have not applied the stringent fiduciary standards to judge employers' actions in the denial of severance pay after a sale of assets, but have uniformly held employers to the "arbitrary and capricious" standard.⁹¹ Derived from pre-ERISA cases involving benefit plan

⁸⁶ See ERISA § 404(a), 29 U.S.C. § 1104(a) (1982).

⁸⁷ Gertner, *supra* note 75, at 276. The fiduciary definition in ERISA is broad enough to "snare" most people involved in the operation or management of a private pension or welfare benefit plan. See *id.* The implication of this breadth is that the professional advisors of the plan, namely the attorneys, accountants and investment personnel working on the plan, may also be fiduciaries of the beneficiaries. See *id.* "ERISA does not prohibit an officer of the sponsor from also serving as trustee; the officer who is a fiduciary by virtue of being a trustee is subject to the fiduciary standards of ERISA section 404." Pianko, *Plan Investments & Fiduciary Liability*, 11 J. PENSION PLANNING & COMPLIANCE 241, 245 (1985). See *Anderson v. Ciba-Geigy Corp.*, 759 F.2d 1518, 1522 (11th Cir.) (Ciba-Geigy executive deemed to be fiduciary, although not named as plan trustee for severance pay determinations), *cert. denied*, 106 S. Ct. 410 (1985); see also Comment, *Arbitrary and Capricious*, *supra* note 15, at 1041-43 (broad definition of fiduciary has "ensnared" traditionally exempt individuals).

⁸⁸ 29 U.S.C. § 1104(a) (1982).

⁸⁹ See *id.*; see also *Struble v. New Jersey Brewery Employees' Welfare Trust Fund*, 732 F.2d 325, 331-32 (3d Cir. 1984); *Donovan v. Cunningham*, 716 F.2d 1455, 1464 (5th Cir. 1983), *cert. denied*, 104 S. Ct. 3533 (1984); see also S. REP. NO. 127, 93d Cong., 2d Sess. 1176, reprinted in 1974 U.S. CODE CONG. & AD. NEWS 4838, 4865-66 (fiduciaries must act in best interest of plan participants).

⁹⁰ See *Struble*, 732 F.2d at 333-34; *Donovan v. Bierwirth*, 680 F.2d 263, 268-70 (2d Cir.), *cert. denied*, 459 U.S. 1069 (1982).

⁹¹ See *Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1148-49 (4th Cir. 1985); *Anderson v. Ciba-Geigy Corp.*, 759 F.2d 1518, 1520-21 (11th Cir.), *cert. denied*, 106 S. Ct. 410 (1985); *Blau v. Del Monte Corp.*, 748 F.2d 1348, 1352-53 (9th Cir. 1984), *cert. denied*, 106 S.

disputes brought under the LMRA,⁹² the standard has typically been applied in cases brought by individual claimants against the trustees of plans, charging that the trustees have incorrectly balanced the interests of present and future claimants.⁹³ Because the courts recognize that trustees should have wide discretion in interpreting the terms of benefit plans, trustee decisions as to who will receive what benefits and when will not be overruled unless proven to have been made arbitrarily and capriciously.⁹⁴ Recent decisions have held this standard applicable in sale-of-assets severance pay claims brought against the employer/trustee regardless of whether or not the employees were financially injured by the sale.⁹⁵ The standard may be more sharply scrutinized by contrasting two recent severance pay cases in which courts seemingly considered themselves compelled to apply the arbitrary and capricious

Ct. 183 (1985); *Sly v. Mallory & Co.*, 712 F.2d 1209, 1211 (7th Cir. 1983). *Cf.* *Gilbert v. Burlington Indus.*, 765 F.2d 320, 329 (2d Cir. 1985) (arbitrary and capricious standard applicable on remand of severance pay claim) (*dicta*). A state court has also adopted the arbitrary and capricious standard of review in severance pay claims. *See Barry v. Dymo Graphic Sys.*, 394 Mass. 830, 835, 478 N.E.2d 707, 713 (1985). *But cf.* *Struble v. New Jersey Brewery Employees' Welfare Trust Fund*, 732 F.2d 325, 333-34 (3d Cir. 1984) (in employee action against formal trust with named trustees, strict ERISA "fiduciary duties" standard, not arbitrary and capricious standard, held applicable to judge trustees' decision). *See generally* Comment, *Arbitrary and Capricious*, *supra* note 15, for a historical review of this standard.

⁹² *See* Comment, *Arbitrary and Capricious*, *supra* note 15, at 1037-41. The arbitrary and capricious standard "evolved" in actions brought under section 302 of the LMRA, 29 U.S.C. § 186 (1982), through the courts' development of a body of federal common law by borrowing fiduciary standards from state law. *See id.* at 1037; *see also* *Music v. Western Conference of Teamsters Pension Trust Fund*, 712 F.2d 413, 418 (9th Cir. 1983) (trustee determinations under ERISA held to same arbitrary and capricious standard derived from LMRA).

⁹³ *See Struble v. New Jersey Brewery Employees' Welfare Trust Fund*, 732 F.2d 325, 333 (3d Cir. 1984). If plan beneficiaries, in an action against trustees, claim that the trustee-fiduciaries have benefited other beneficiaries at their expense, the arbitrary and capricious standard is appropriate. *See id.* However, if the claimants charge that their employer-trustees have benefitted themselves or third parties by not disbursing the benefit funds allegedly due, the allegation requires review under a more stringent fiduciary loyalty standard. *See id.* at 333-34; *supra* note 90 and accompanying text.

⁹⁴ *See Sly v. Mallory & Co.*, 712 F.2d 1209, 1211 (7th Cir. 1983); *cf.* *United States Mine Workers v. Robinson*, 455 U.S. 562, 573 (1982) (LMRA action using standard will not hold fiduciaries liable unless they acted arbitrarily toward beneficiaries).

In *Anderson v. Ciba-Geigy Corp.*, 759 F.2d 1518, 1522 (11th Cir.), *cert. denied* 106 S. Ct. 410 (1985), the Court of Appeals for the Eleventh Circuit listed three factors to be considered in determining whether an employer's action was arbitrary and capricious: "(1) uniformity of construction; (2) fair reading and reasonableness of that reading; and (3) unanticipated costs." *Id.* (citation omitted). The employees could not meet the burden of proving that any of these factors had been "obviously infringed" therefore, the court affirmed summary judgment for the defendant corporation. *See id.*

⁹⁵ *See supra* notes 82 & 92 and accompanying text.

In *Jung v. FMC Corp.*,⁹⁶ FMC had sold its Engineered Systems Division to ESD Corporation, a wholly owned subsidiary of a third corporation.⁹⁷ As part of the sale agreement, ESD agreed to offer employment to all former FMC employees at "a comparable salary" and with substantially the same benefits as they were receiving from FMC, including the retention of seniority for severance pay.⁹⁸ After the sale, the employees brought a claim for severance pay under the severance policy provisions of their employee manual.⁹⁹ The Ninth Circuit, applying the arbitrary and capricious standard, found that FMC's denial of severance pay was a reasonable interpretation of its severance policy, and therefore not arbitrary and capricious.¹⁰⁰ The court suggested that to allow severance benefits when employees have not suffered financial loss would be to allow a windfall double recovery,¹⁰¹ a result not favored by the

⁹⁶ 755 F.2d 708 (9th Cir. 1985).

⁹⁷ See *id.* at 709.

⁹⁸ See *id.* In *Jung*, after the sale of assets, the FMC employees retained their jobs, benefits and seniority. *Id.* The seniority factor becomes important when employees are not awarded severance pay after their company sells its assets. Because severance pay is generally paid on the basis of years of employment, see Note, *supra* note 9, at 596, employees who do not retain their seniority with the purchasing company have necessarily forfeited their accumulated severance pay. If, however, they retain their seniority with the purchasing company under the same benefit plan, the employees have the potential to collect severance pay for their entire time of employment—the years spent with the first employer, plus the time spent with the second, resulting in a "double recovery." See *Jung*, 755 F.2d at 714.

⁹⁹ See *Jung*, 755 F.2d at 709-10.

¹⁰⁰ See *id.* The employees claimed that they were "terminated" from employment with FMC, even though they continued working for the same salary at the same jobs. See *id.* The FMC "Policy Guide" was similar to the employment manuals analyzed in common law state cases in that "[n]othing in the Policy Guide refers to a termination resulting from a sale of business." *Id.* at 712.

The *Jung* court adopted the arbitrary and capricious standard of review, rejecting the employees' suggestion that the court apply the strict ERISA fiduciary standard enunciated in section 404(a), as applied in *Struble v. New Jersey Brewery Employees' Welfare Trust Fund*, 732 F.2d 325 (3d Cir. 1984). See *Jung*, 755 F.2d at 711; see *supra* note 83 (selected text of 404(a)); *supra* note 93 (*Struble* differentiation of standards). After distinguishing the facts in *Struble*, the *Jung* court ruled that "[w]hatever may be the appropriate standard of review in cases like *Struble*, the arbitrary and capricious standard seems adequate" for this case. See *Jung*, 755 F.2d at 711.

The *Jung* court implied that this standard was appropriate because FMC was entitled to deference when the employees suffered no loss due to their sale to EDS. See *Jung*, 755 F.2d at 712, 714. The court analyzed the manual and found that implicit in its language was the notion that an employee must actually be "out of work" to collect severance pay. See *id.* at 713. The fact that FMC's employees suffered no financial loss due to the sale was noted by the *Jung* court as a factor in their determination that the employers did not act arbitrarily. See *id.* at 714.

¹⁰¹ See *Jung*, 755 F.2d at 714. If they were to receive severance pay, the employees "would receive benefits based upon employment with FMC both at the time of divestiture

policy considerations underlying ERISA.¹⁰²

In *Anderson v. Ciba-Geigy Corp.*,¹⁰³ Ciba-Geigy had agreed to provide severance pay to employees terminated without cause.¹⁰⁴ The plaintiffs' division was subsequently sold to Communications Technology Company, but the purchaser refused to take on any of the liabilities of Ciba-Geigy.¹⁰⁵ Although the employees retained their jobs and salaries, seniority rights and vacation benefits were lost.¹⁰⁶ After Ciba-Geigy refused to provide severance pay, the employees sued.¹⁰⁷ Deciding in favor of the corporation, the court stated that "[ERISA] provides for judicial review of benefit deter-

and presumably again if subsequently laid off. . . ." *Id.* To allow employees to collect severance pay at the time of the sale, and an overlapping amount should they become terminated from EDS, would have been a "windfall" which is not supported by the policies of ERISA. *See id.* at 714; *accord* *Sly v. Mallory & Co.*, 712 F.2d 1209, 1211 (7th Cir. 1983) (awarding severance pay when employees suffer no loss is "windfall" not in keeping with policies of ERISA). Thus, it is suggested that recent courts are looking to events *after* the sale of assets in determining the merits of employee claims for severance pay. At common law, this generally was not the case. *See supra* note 17-18 and accompanying text; *see also* *Willets v. Emhart Mfg. Co.*, 152 Conn. 487, 489, 208 A.2d 546, 548 (1965) (severance pay concerns the past, not future events after the sale of assets).

¹⁰² *See Jung*, 755 F.2d at 714. "[O]ne of the goals of ERISA was to keep plans within reasonable costs and that, although there is no prohibition of double recovery under ERISA, policy considerations behind ERISA suggest that double recovery should not be favored." *Id.*; *accord* *Sly v. Mallory & Co.*, 712 F.2d 1209, 1211 (7th Cir. 1983); *cf.* *Grubbs, supra* note 3, at 8-9 (expressing concern over corporate disincentives to participate in ERISA plans).

¹⁰³ 759 F.2d 1518 (11th Cir.), *cert. denied*, 106 S. Ct. 410 (1985).

¹⁰⁴ *See id.* at 1520. The Ciba-Geigy plan stated that employees would receive severance pay if they became terminated "for reasons beyond the control of the employee (e.g., reorganization, budgetary cutback, lack of work, . . .)." *Id.* The plan also stated, however, that the severance pay provision would not apply in any "special situation." *Id.* The meaning of this phrase was not included in the Ciba-Geigy manual. *See id.*

¹⁰⁵ *See id.*

¹⁰⁶ *See id.* The loss of vacation and seniority rights meant that unlike the employees in *Jung*, *see supra* note 98 and accompanying text, the *Anderson* employees suffered financial injury as a result the sale of their company. *See id.*; *see also supra* notes 14 & 98 (loss of seniority rights equates to loss of accumulated severance benefits should purchasing company liquidate).

¹⁰⁷ *See Anderson*, 759 F.2d at 1520. In *Anderson*, there was no named "fiduciary" or trustee who maintained the severance pay plan, because payments were to be disbursed from the general assets of the corporation. *See Anderson*, 759 F.2d at 1522. The *Anderson* court ruled that the Ciba-Geigy executive who interpreted his company's severance pay plan was the employees' fiduciary trustee when he decided to deny their claim. *See id.*; *see also supra* notes 83-88. This situation seems to be typical of unfunded severance pay plans. *See Gilbert v. Burlington Indus.*, 765 F.2d 320, 325-26, 328 (2d Cir. 1985) (unfunded severance pay plan payable from employer's general assets with no "named fiduciary"); *Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1502, 1504 (9th Cir. 1985) (same); *cf. Donovan v. Dillingham*, 688 F.2d 1367, 1372-73 (11th Cir. 1982) (formally funded plan in writing "not prerequisite to coverage under" ERISA).

minations . . . using the arbitrary and capricious standard."¹⁰⁸ Since the employees were unable to prove that the corporation's decision was arbitrary, they could not recover even though they suffered financial loss due to the sale.¹⁰⁹ While both the *Jung* and *Anderson* decisions used the same standards to reach the same result, the singular fact that in *Anderson* the employees suffered financial injury was not considered a relevant factor in the determination of that case.¹¹⁰

It is suggested that the arbitrary and capricious standard is not the only correct standard to apply in ERISA governed severance pay cases.¹¹¹ In situations similar to the facts of the *Jung* case, use of this standard appears equitable.¹¹² However, in situations similar to the facts of the *Anderson* case, in which inequities would result by forcing financially injured employees to meet an almost insurmountable burden,¹¹³ the arbitrary and capricious

¹⁰⁸ See *Anderson*, 759 F.2d at 1520-21. The court referred to the arbitrary and capricious standard as the "statutory standard." *Id.* But see *infra* note 118 and accompanying text.

¹⁰⁹ See *id.* at 1523. "In sum, plaintiffs have presented no evidence sufficient to establish that Kase's decision to deny severance pay was arbitrary and capricious. Even though plaintiffs have suffered an 'injury' through a loss of some benefits, neither ERISA nor the Ciba-Geigy Employee Benefit Plan has been violated." *Id.* It is suggested, however, that the spirit of ERISA has been usurped by the *Anderson* court's rigid adherence to the application of the arbitrary and capricious standard when employees are injured by a sale of assets. See *infra* notes 112, 114-15 and accompanying text.

¹¹⁰ Compare *Anderson*, 759 F.2d at 1523, with *Jung*, 755 F.2d at 708-10.

¹¹¹ *Blau v. Del Monte Corp.*, 748 F.2d 1348, 1353 (9th Cir. 1984), *cert. denied*, 106 S. Ct. 183 (1985). Cf. *Struble v. New Jersey Brewery Employees' Welfare Trust Fund*, 732 F.2d 325, 331-33 (3d Cir. 1984) (court applied "strict statutory standards of ERISA," not arbitrary and capricious standard, in non sale-of-assets employee action against trustee). It seems neither logical nor equitable to contend that the "fiduciary" standards set out explicitly in ERISA, see *supra* note 6, can never apply to severance pay claims brought by financially injured employees. Moreover, it can be argued that Congress has allowed federal courts leeway to develop an equitable body of federal common law in the employee benefits arena. See *supra* notes 78-81 and accompanying text. The notion, therefore, that courts are "bound" to accept the applicability of the arbitrary and capricious standard as the *only* appropriate ERISA standard, does not seem logically correct. Cf. *Struble*, 732 F.2d at 333-34 (court rejected arbitrary and capricious standard).

¹¹² See *Jung v. FMC Corp.*, 755 F.2d 708, 710-11 (9th Cir. 1985). In *Jung*, the arbitrary and capricious standard from the LMRA thwarted a possible double recovery by the employees. *Id.*; see also *Sly v. Mallory & Co.*, 712 F.2d 1209, 1211 (7th Cir. 1983) (LMRA standard applied to prevent double recovery); cf. *Music v. Western Conference of Trustees' Pension Trust Fund*, 712 F.2d 413, 418 (9th Cir. 1983) (LMRA arbitrary and capricious standard applicable to ERISA claims).

¹¹³ See *Anderson*, 759 F.2d at 1523. The *Anderson* opinion seemed to imply that although employees were injured by a sale of assets, courts are nonetheless *compelled* to apply the arbitrary and capricious standard to their claim. See *id.* at 1521. When courts have

standard should not be applied. The policy and legislative history of ERISA strongly suggest that employer economic gains at the expense of employees and their welfare benefit plans must not be tolerated.¹¹⁴ By applying the arbitrary and capricious standard in every decision, considering neither the employee's financial position nor the theoretical underpinnings of applying the standard, the courts have simply failed to create an equitable body of federal common law in the severance pay arena.

A Modified Approach

In this new area of the law, a more flexible approach is needed to create an equitable harmony between the pro-employee decisions at common law¹¹⁵ and the pro-employer decisions under ERISA.¹¹⁶ Employers who unilaterally adopt severance pay plans assume the risk of having to disburse funds under the agreement if a triggering event should occur,¹¹⁷ and ERISA must not nullify this. However, ERISA should not be used to create a windfall for employees who have suffered no loss.¹¹⁸ It is suggested, therefore,

chosen this standard in adjudicating severance pay claims after a sale of corporate assets, the employees typically lose because they cannot meet this heavy burden of proof. See *supra* note 8 (severance pay cases applying arbitrary and capricious standard predominately have employer emerging victorious). This situation is suggested to be inequitable, since federal courts have the power to create ERISA common law to remedy the employee injury situation; for courts to assert that they are "bound" to one standard, even when injured employees are forced to prove their employers acted arbitrarily, is flawed reasoning.

¹¹⁴ See *House Report, supra* note 2, at 4639-43. The language in ERISA clearly states that the intent of Congress was to "protect the interests of employees." ERISA § 2(b), 29 U.S.C. § 1001(b) (1982). The mere fact that an employer may realize a "gain" by not disbursing severance pay if employees have not become eligible for it is obviously not prohibited by ERISA, nor should it be. See *Jung*, 755 F.2d at 714 (one goal of ERISA was to keep benefit plans within reasonable costs for employers); Grubbs, *supra* note 3, at 9 (disincentives may drive employers away from maintaining these voluntary ERISA plans). However, it is also an ERISA goal to thwart employee loss. See *House Report, supra* note 2, at 4639-43. These two goals are in no way mutually exclusive; they can work together, it is suggested, by applying a standard other than "arbitrary and capricious" to cases in which employees injury occurs. See *infra* notes 126-32 and accompanying text.

¹¹⁵ See *supra* note 11 and accompanying text.

¹¹⁶ See *supra* note 8.

¹¹⁷ See J. CALAMARI & J. PERILLO, *supra* note 26, at §§ 4-15. The common law notion that a unilateral contract obligation is produced by a severance pay provision in employee manuals, see *supra* note 26, has not been challenged in recent decisions. See *supra* note 8; *Fletcher v. Amax Inc.*, 160 Ga. App. 692, 694, 288 S.E.2d 49, 51 (1981); *Dulany Foods Inc. v. Ayers*, 220 Va. 502, 505, 260 S.E.2d 196, 199 (1979). Severance pay decisions falling under ERISA, see *supra* note 8, also do not challenge this common law notion.

¹¹⁸ *Accord Jung*, 755 F.2d at 714; *Sly v. Mallory & Co.*, 712 F.2d 1209, 1211 (7th Cir. 1983); *Younger v. Thomas Int'l Corp.*, 275 Ark. 327, 329, 629 S.W.2d 269, 274 (1982); *Linz v.*

that courts employ a dual standard approach, with the financial position of the employee after the sale being the determining factor in the selection of ERISA standards.¹¹⁹

To the extent that employees suffer no financial injury due to the sale, and more specifically, no loss of seniority rights triggering a permanent loss of accumulated severance pay benefits,¹²⁰ the arbitrary and capricious standard is adequate.¹²¹ This standard has been accepted by courts in the field of labor for many years,¹²² and

Champion Int'l Corp., 675 P.2d 979, 980-81 (Mont. 1984).

¹¹⁹ Increasingly, courts have moved away from the common law approach of considering only events that have transpired between the parties prior to the sale of assets. *See, e.g., Jung*, 755 F.2d at 714 (financial impact of sale upon employees taken into account in decision); *Sly v. Mallory & Co.*, 712 F.2d 1209, 1211 (7th Cir. 1983) (same). This has been limited, however, to taking into account the fact that employees have had *no* financial injury after the sale in denying such claims. *See supra* notes 101-02. It is asserted that this trend of weighing events after the sale be extended to instances where employees *are* financially injured due to the sale; this position ought to determine the applicable standard in the adjudication.

¹²⁰ *See e.g., Jung*, 755 F.2d at 709 (employees offered comparable salary, benefits, and retained seniority, suffering no financial loss). *See also supra* note 99.

¹²¹ *See Jung*, 755 F.2d at 709; *see supra* notes 101-02. To the extent that employees suffer no loss due to the sale of their employer's assets, *see supra* note 14, it is suggested that the arbitrary and capricious standard, already judicially accepted in severance pay adjudications, is the most equitable standard. *See supra*, note 8 (cases exemplify wide judicial acceptance of arbitrary and capricious standard). This standard forces employees to show that they have in fact suffered injury as a result of their employer's actions in order to recover. *See Jung*, 755 F.2d at 712-14 (employees without injury should not benefit from relaxing stringent standards). The scenario of employees collecting severance pay once at the time of "technical termination" from their jobs, with no loss of pay or benefits due to the sale, and subsequently collecting an overlapping severance amount from the purchasing company if they become terminated, is a "double recovery" which would cause a disincentive for companies to maintain ERISA plans. *See id.* at 714; *see supra* notes 101-02.

A second argument for this proposal can be made. The modern understanding of a severance payment is a benefit which tides an employee over until he or she finds a new job. *See Gallagher, supra* note 10, at 34; *see supra* notes 17-18 and 51 (suggesting modern view of severance pay is analogous to unemployment benefits). If an employee keeps the same job, *and* retains the same seniority and benefits with the purchasing company, the employee has lost nothing due to the sale, and has not in fact become "unemployed" due to the change in employers. *See Petrella v. NL Indus.*, 529 F. Supp. 1357, 1361 (D.N.J. 1982); *Pinto v. Zenith Radio Corp.*, 480 F. Supp. 361, 363 (N.D. Ill. 1979), *aff'd mem.*, 618 F.2d 110 (7th Cir. 1980); *Younger v. Thomas Int'l Corp.*, 275 Ark. 327, 330, 629 S.W.2d 294, 296 (1982) *Linz v. Champion Int'l Corp.*, 675 P.2d 979, 981 (Mont. 1984). Therefore, it seems that employers should continue to enjoy the deference which the arbitrary and capricious standard gives them when the employers contract with a purchasing company so that their employees are not injured, or indeed "terminated," because of the sale.

¹²² *See Danti v. Lewis*, 312 F.2d 345, 348 (D.C. Cir. 1962) (trustee's decision judged against arbitrary and capricious standard); *Insley v. Joyce*, 330 F. Supp. 1228, 1234 (N.D. Ill. 1971) (same). *See generally* Comment, *Arbitrary and Capricious, supra* note 16, at 1036-41 (historical application of arbitrary and capricious standard).

its continued application in cases in which employees have suffered no loss will force employees to prove a real injury before "double recovery" is allowed.¹²³

If employees do suffer a financial loss, however, the employers should be held to the strict fiduciary standards set forth in section 404(a) of ERISA,¹²⁴ not the more deferential arbitrary and capricious test. Because severance pay plans are typically bankrolled by employers' general assets and are thus "unfunded,"¹²⁵ the plans may not have the "appointed trustees" required by ERISA for "funded" plans.¹²⁶ Thus, the executive who decides whether to disperse severance pay is usually deemed the "trustee" for ERISA purposes.¹²⁷ It is suggested that an inevitable conflict of interest is created by the tension between the officer's corporate duty to retain corporate assets, and the officer's concurrent fiduciary duty to thwart financial harm to the employees mandated by ERISA. The deferential standard adopted from the LMRA was not created to deal with this situation.¹²⁸ Instead, the standard was adopted to give trustees discretion in interpreting benefit plans, not to give corporations deferential treatment in retaining earnings at the expense of truly injured beneficiaries. It seems essential, therefore, in cases in which employees suffer a financial loss after a sale of assets, for the executive to be held to meet the fiduciary standard of

¹²³ See *supra* note 122 and accompanying text.

¹²⁴ 29 U.S.C. § 1104(a) (1982); see *supra* note 6 for selected text.

¹²⁵ See ERISA § 301(a)(1), 29 U.S.C. § 1081(a)(1) (1982) (exempting "welfare benefit plans" from funding requirement). Since there is no funding requirement for an ERISA employee welfare plan, the severance pay plans that have generated judicial review have typically been unfunded and not set apart from the corporation's general assets. See *Holland v. Burlington Indus., Inc.*, 772 F.2d 1140, 1145 (4th Cir. 1985); *Gilbert v. Burlington Indus.*, 765 F.2d 320, 324 (2d Cir. 1985); *Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1502 (9th Cir. 1985); *Sly v. Mallory & Co.*, 712 F.2d 1209, 1213 (7th Cir. 1983).

¹²⁶ ERISA § 402(a), 29 U.S.C. § 1102 (1982). While the statute requires appointed trustees for funded plans, see *id.*, courts have held that no appointed trustee is required in unfunded plans. See, e.g., *Anderson*, 759 F.2d at 1522 (no corporate appointed severance plan trustee, thus court selected corporate executive as trustee); *Gilbert*, 765 F.2d at 328 (same). See also *supra* note 108.

¹²⁷ See *supra* note 88.

¹²⁸ See *Pianko*, *supra* note 87, at 245. "As a fiduciary, the officer must act exclusively for the purpose of providing benefits to plan participants . . ." *Id.* Thus, the test to adjudicate the claims of injured employees should be to ascertain whether the "appointed" trustee has discharged "his duties with respect to the plan solely in the interest of the participants . . ." ERISA § 404(a)(1), 29 U.S.C. § 1104(a)(1) (1982). See also *Gertner*, *supra* note 75, at 280-81 ("the duty of trustees is to act solely in the interest of plan participants . . . even if those interests are . . . in conflict with the interests of the plan sponsor . . .").

a trustee.¹²⁹

Judicial acceptance of this dual standard is suggested so that the common law of ERISA can become equitable to both employer and employee. The main Congressional purpose in enacting ERISA was to *protect* employees by creating regulations by which private companies must run their benefit plans.¹³⁰ Because there is no requirement that these companies establish benefit plans, some believe that the breadth and complexity of the regulations have actually created disincentives for the operation of benefit plans.¹³¹ To the extent that courts were to completely reverse their current position and impose the strict fiduciary standard to *every* ERISA adjudication, companies would be unable to take advantage of the deferential arbitrary and capricious standard, even in those instances in which that standard would be more appropriate.¹³² This additional layer of corporate disincentives, added to an already complex ERISA field, would ultimately injure employees because of the eventual decline in the number of companies participating in benefit plans.

CONCLUSION

Employee claims for severance pay in the corporate sale of assets situation have entered a dramatic new phase. At common law, employees were usually granted relief by state courts no matter what their financial position after the sale. However, since ERISA

¹²⁹ See Comment, *Arbitrary and Capricious*, *supra* note 15, at 1035-41 (arbitrary and capricious standard developed well before enactment of ERISA in 1974 to deal with pension disputes involving named trustees).

¹³⁰ See *House Report*, *supra* note 2, at 4639-42. The policy, declared in ERISA, was to protect "the interests of participants in employer benefit plans . . ." ERISA § 2(b), 29 U.S.C. § 1001(b) (1982).

¹³¹ See Grubbs, *supra* note 3, at 8-9 (some fear ERISA complexity may lead to ultimate discontinuance of benefit plans).

¹³² See *Jung*, 755 F.2d at 711-12. The *Jung* court suggested that the corporate employers were entitled to take advantage of the deferential arbitrary and capricious standard, because the workers suffered no monetary loss as a result of the merger. See *id.* at 714. It is suggested that in this type of situation, the standard was indeed more appropriate than holding the employer to the strict duty of loyalty enunciated in ERISA. Another situation contemplated by this author in which the arbitrary and capricious standard would be more appropriate than the loyalty standard is a situation in which, given two similarly situated employees in a corporation that has merged with another, one employee receives severance pay and the other is denied. The necessity to judge the nature of the different treatment cries out as the primary concern of a just judicial system. Thus, it seems that the arbitrary and capricious standard is also more applicable in situations where corporations deal differently with similarly situated employees.

has been interpreted to envelop the area of severance pay, employees rarely recover, regardless of their losses due to the sale. These inequities necessitate change. The use of a dual standard in adjudicating severance pay claims brought under ERISA can create an equitable situation by thwarting employee double recovery, yet holding employers to a high standard of fiduciary loyalty when employees are financially injured.

Lawrence A. Pasini