

U.S. Department of Labor

Pension and Welfare Benefits Administration
Washington, D.C. 20210



November 14, 1995

95-28A

Mr. Patrick C. Wheeler
Counsel
Kimberly-Clark Corporation
P.O. Box 619100
Dallas, Texas 75261-9100

Dear Mr. Wheeler:

This is in response to your request for an advisory opinion regarding the applicability of Title I of the Employee Retirement Income Security Act of 1974 (ERISA). Specifically, you ask whether the Midwest Express Career Pilot Severance Plan (the Plan) constitutes an "employee welfare benefit plan" under section 3(1) of ERISA, rather than an "employee pension benefit plan" under section 3(2) of ERISA.

Your correspondence and the materials you forwarded to the Department of Labor (the Department) contain the following facts and representations. Midwest Express Airlines, Inc. (Midwest) intends to establish the Plan, effective as of January 1, 1995, to provide a severance benefit to certain of its pilots who have been involuntarily terminated from employment with Midwest as a consequence of losing their airman certificates for failure to meet certain requirements of Federal Aviation Administration (FAA) regulations, or for being ineligible for cockpit positions because of attaining age 60. The Plan will be the only severance benefit provided by Midwest to its pilots, and Midwest intends to fund the Plan out of its general assets.

According to the Plan document, which you have submitted, the Plan will be administered by a Plan Committee, consisting of the President of Midwest and such other individuals as the President selects, that will be responsible for the management, operation, and administration of the Plan. The Plan will provide a lump sum, cash severance payment to full-time pilots who have earned at least 10 years of service, are either a Captain or First Officer, and have been involuntarily terminated from employment with Midwest because of:

- (a) A Participant's failure to hold an appropriate current airman certificate as required under [FAA regulation] 121.383(a)(1), excluding any such failure as a result of cause;
- (b) A Participant's failure to hold a current airman medical certificate under [FAA regulation] 121.383(a)(2), excluding any such failure as a result of (i) the use of alcohol, drugs, or narcotics, or any violation of an alcohol, drug, or narcotics testing program, (ii) willful self-inflicted injury or (iii) such condition is incurred as a result of or incidental to a felonious act perpetrated by the Participant; or
- (c) Attaining age 60 under [FAA regulation] 121.383(c).

Plan document, section 2.11.

The Plan document further provides a schedule for determining the amount of the severance payment, under which the maximum possible payment is 56% of the pilot's annual compensation in the calendar year prior to termination of employment. The lump-sum payment ordinarily will be made in January following the year of termination, but the pilot may, with the consent of the Committee, elect to defer receipt so long as the lump-sum payment is made within 24 months after the termination of the pilot's employment.

You further represent that under the pension programs presently available to Midwest pilots, a normal retirement benefit is payable at age 65 and an early retirement benefit is payable at age 55 (such benefit is reduced actuarially for participants with less than 10 years of service, and is partially subsidized for participants who have earned 10 years of service). The pension program also provides a disability benefit for any participant who has earned at least 5 years of service and who becomes permanently and totally disabled. Pilots who retire after age 55 or on disability are eligible for continued medical and life insurance coverage in retirement. You emphasize that the severance benefit payable under the Plan is intended to be limited to those eligible pilots who suffer an involuntary termination of employment and is not intended to be available to pilots who voluntarily terminate employment for any reason, including retirement.

Section 3(1) of Title I of ERISA defines the term "employee welfare benefit plan" to include, inter alia, employer- or employee-organization-sponsored programs that are established or maintained to provide "any benefit described in section 302(c) of the Labor Management Relations Act, 1947 [29 USCS section 186(c)] (other than pensions on retirement or death, and insurance to provide such pensions)." Among the benefits described in section 302(c) of the Labor Management Relations Act, as of the time ERISA was enacted, is severance pay.

The term "employee pension benefit plan" is defined in section 3(2) of Title I of ERISA to include any employer- or employee-organization-sponsored program "that by its express terms or as a result of surrounding circumstances . . . provides retirement income to employees, or . . . results in a deferral of income by employees for periods extending to the termination of covered employment or beyond, regardless of the method of calculating the contributions made to the plan, the method of calculating the benefits under the plan or the method of distributing benefits from the plan."

Section 3(2) further permits the Secretary of Labor by regulation to prescribe rules "consistent with the standards and purposes of [ERISA] providing one or more exempt categories under which . . . severance pay arrangements, . . . shall, for purposes of this title, be treated as welfare plans rather than pension plans."

The statute clarifies, however, in section 3(2)(B), that:

In the case of any arrangement or payment a principal effect of which is the evasion of the standards or purposes of this Act applicable to pension plans, such arrangement or payment shall be treated as a pension plan.

Thus, in accordance with section 3(2)(B), the Department has the authority to set standards to determine whether severance pay arrangements should be treated as employee welfare benefit plans under section 3(1), rather than as employee pension benefit plans under section 3(2).

Regulation section 29 C.F.R. 2510.3-2(b) sets forth certain criteria that the Department has determined characterize severance pay arrangements that are not employee pension benefit plans within the meaning of section 3(2) of Title I of ERISA. The "safe harbor" criteria are: (1) that the severance payments are not contingent, directly or indirectly, on the employee's retiring; (2) that the total amount of such payments does not exceed the equivalent of twice the employee's annual compensation during the year immediately preceding the termination of his service; and (3) that payments are completed within 24 months after the termination of the employee's service.¹

¹ Your letter does not indicate that the Plan's benefits are to be made in connection with a limited program of terminations. Thus, this opinion will not address the criteria set forth in regulation section 2510.3-2(b)(1)(iii)(A).

In 1979, in amending regulation section 2510.3-2(b) (effective retroactive to January 1, 1975) to enlarge the amount and duration of payments recognized in the second and third criteria to their present scope, the Department commented on its intent in establishing the safe harbor:

The proposed amendment was not intended to differentiate or to cause a differentiation between severance benefits paid to employees who happen to retire after termination, and severance benefits paid to employees who do not retire. Rather, the provision . . . was intended to exclude from the safe harbor programs of payments which are made because of, or which are conditional upon, an employee's retiring, since such payments would seem to constitute retirement income rather than severance pay. Thus, the amendment . . . makes clear that the status of severance payments under the regulation does not depend upon whether the recipient of the payments has retired, so long as he is not required, directly or indirectly, to retire in order to receive the payments. It should be noted that, under this provision, the protection of the safe harbor would be unavailable not only if the benefits were explicitly made contingent upon retirement but also if the surrounding circumstances were such that the benefits were, in practice, paid only to employees who had reached retirement age.

March 2, 1979 Preamble to Amendment to 29 C.F.R. § 2510.3-2(b), 44 Fed. Reg. 11762 (1979).

Your representations and documents indicate that the Plan appears to comply with the second and third of the safe harbor criteria. You represent, first, that the total amount of payments to any pilot under the Plan will not in any case exceed the equivalent of twice the pilot's annual compensation during the year immediately preceding the termination of his service. Second, although the Plan permits some deferral of the lump sum payment, you represent that it must be paid, in all cases, within 24 months of the pilot's termination from employment, the event causing the pilot to have a right to a benefit.

With regard to the first criterion, it is the view of the Department that the Plan does not appear by its terms to make the payment of benefits "contingent, directly . . . , upon the employee's retiring." The Plan provides that benefits are payable only if a pilot's employment is involuntarily terminated due to loss of the airman certificate for one of the specified reasons, or due to attaining age 60. Although a pilot may be eligible for, and may in fact, retire after having been involuntarily terminated, the payment of benefits under the terms of the Plan is contingent only upon that involuntary termination. Thus, the Plan does not pay benefits in any case in which a pilot chooses, independently, to retire, although not required to terminate service for one of the reasons that triggers severance benefits. Also, the Plan permits payment of benefits to some individuals who are younger than the retirement eligibility ages available to the pilots as a group, although those individuals may be eligible for disability retirement. These factors lead us to conclude that the Plan by its terms does not expressly pay benefits "only to employees who ha[ve] reached retirement age" and that the terms of the Plan do not demonstrate that the Plan is necessarily intended to provide retirement income to employees. Accordingly, it is the opinion of the Department that the Plan you describe may satisfy the requirements for the safe harbor in regulation section 2510.3-2(b) and may be viewed as an "employee welfare benefit plan" within the meaning of section 3(1) of ERISA and not an "employee pension benefit plan" within the meaning of section 3(2)(A) of ERISA.

We note, however, that the safe harbor is not available if the severance benefits are "indirectly" contingent on the employees' retirement. As described in the Preamble to the regulation, benefits are "indirectly" contingent on retirement when benefits are in practice paid only to employees who have reached retirement age. Here, the Plan imposes a minimum service requirement of 10 years of service for payment of severance benefits, which is the same amount of service credit required for full vesting under the pension program available to the pilots, and more than enough service for eligibility for disability retirement. It is therefore possible, as a result of surrounding circumstances, that the Plan may in fact provide benefits to many employees who are eligible for retirement. Although this fact alone is not sufficient to require the Plan to be treated, by its terms, as a pension plan, if the actual payment of severance benefits under the Plan predominantly coincides with the voluntary retirement of the

recipients, the Plan may be required to be treated as a pension plan because those additional circumstances could indicate that the Plan systematically provides retirement income to employees and thus that the severance benefits are indirectly contingent on retirement.

This letter constitutes an advisory opinion under ERISA Procedure 76-1. Accordingly, it is issued subject to the provisions of the procedure, including section 10 thereof relating to the effect of advisory opinions.

Sincerely,

ROBERT J. DOYLE
Director of Regulations and Interpretations