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NO SEVERANCE PAY FOR CONSTRUCTIVE TERMINATION

by
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A federal appeals court has concluded that executives were not entitled to severance pay because they were not involuntarily terminated, but were instead, at least arguably, constructively discharged. The case is *Mallon v. Trust Co. of New Jersey Severance Pay Plan*, 2008 WL 2553027 (3d Cir. 2008). The federal Court of Appeals for the Third Circuit, in an unpublished decision, upheld a severance plan administrator's denial of benefits to executives who claimed they were constructively discharged by reason of a reduction in their duties and compensation. In doing so, the court applied a somewhat heightened standard of review due to a conflict of interest resulting from the severance plan being funded from the employer's general corporate assets.

The executives worked for a trust company that was acquired by a bank. The bank offered all the executives employment, and the executives accepted those offers. The executives contended, however, that the conditions of their employment changed substantially and detrimentally following the acquisition. One executive asserted, for example, that he was demoted from senior vice president to regional vice president, and the others claimed they were demoted from regional sales managers to account executives. More generally, the executives alleged that their managerial and supervisory duties were significantly reduced. The executives had worked in residential mortgage lending with the trust company, and claimed that the acquiring bank decided to deemphasize that line of business. As a result, the executives' commissions declined, and this was particularly important because the executives asserted that their compensation was largely determined by commissions. A couple of months following the merger, the executives notified the bank that they deemed themselves constructively discharged because the bank had detrimentally changed their duties, responsibilities, job titles, and compensation, and that those changes were tantamount to a termination of employment.

After notifying the bank that they believed they had been constructively discharged, the executives filed claims for severance benefits. Those claims were denied, in part because the plan administrator said benefits were payable only upon involuntary termination by the company, and not in the event of a constructive discharge. The plan language described the individuals eligible for benefits as those employees whose employment is "involuntarily terminated by the company" in certain circumstances. The court determined that even under a heightened standard of review, the plan administrator's decision that no benefits were payable in the event of a constructive termination was reasonable.

" [F]or those plans . . . that do not intend to provide benefits in the case of constructive discharge, it might be well to say so explicitly . . . ."

The court went on to make an interesting point about another plan provision. Under the plan's terms, even if an employee were involuntarily terminated by the company in one of the circumstances triggering benefits, no amount would be payable if the employee were offered employment by the company that was comparable to the employee's then current position and the employee were to refuse that employment. The court said an employee must, in fact, refuse the offered employment to be able to argue that it was not comparable. In other words, under the plan's terms, it would be necessary to consider whether there was an offer of comparable employment only if the employee were to decline that continued employment. If an involuntarily terminated employee were to accept a new position offered to him or her, the court seemed to suggest that the employee would not then be in a position to argue that the position was not comparable. This may be a misreading of the court's opinion, but if not, it seems surprising. It would eliminate the ability of an executive who believes he or she is being offered comparable employment to later complain that, in fact, the position was not comparable. Leaving aside whether an executive would, in that circumstance, have an argument that he or she is entitled to a comparable position – for example, where there is an employment contract with representations about the employee's promised duties, compensation, and other aspects of employment – it would seem surprising if an executive who believes he or she is being offered comparable employment (and, as a result, is not eligible for severance benefits) could not argue that the position turned out, in fact, not to be comparable, and that the executive is therefore entitled to severance benefits.

Lessons. It is a challenge to know how much detail to include in a plan document. There are, however, enough court cases dealing with employees' entitlement to severance pay in the event of constructive discharge that it may be worth addressing the point in the plan document. Some plans do so by indicating that benefits will be payable not only in the event of certain involuntary terminations without cause, but also where an executive terminates employment for "good reason." But for those plans, like the one at issue in the *Mallon* decision, that do not intend to provide benefits in the case of constructive discharge, it might be well to say so explicitly, rather than relying only on language that refers to "involuntary termination" by the employer. One might do so by expressly stating that benefits will be payable upon involuntary termination by the employer, and not in the case of any "constructive discharge," "constructive termination," or termination by the employee for "good reason" (or any other reason).

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