



FRANK STEINBERG'S
SMART
ENTREPRENEUR'S
GUIDE TO
SEVERANCE
AGREEMENTS

Written and Published as an Educational Service by

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Key Questions and Answers About Severance Agreements

❖ What is a Severance Agreement?

A Severance Agreement is a contract between an employer and an employee, usually an executive, that ends the employment relationship.

In the agreement, the employer promises to give the executive certain benefits. These may include money -- in the form of a lump sum payment, ongoing salary or ongoing healthcare premiums (COBRA) -- outplacement services, and perhaps a good letter of reference.

In exchange, the executive releases the employer from all legal claims the executive may have, including claims for disputed wages or bonuses, wrongful discharge and discrimination.

For a Severance Agreement to be enforceable, the employer must give the executive something more than what he is already entitled to. For example, it is not enough for an employer to ask for a release from an executive in exchange for wages, salaries, commissions, bonuses and vacation pay that the executive has already earned.

❖ What should a Severance Agreement include?

The Severance Agreement may cover some or all of the following:

Financial Components

- Severance, commission, bonus, and deferred compensation plan payouts due.
- Accrued vacation and sick time payouts due.
- Rights under pension, profit sharing, and 401(k) plans.
- Stock options statement and exercise schedule.
- Loans to an employee.
- Business expenses paid by the employee and not yet reimbursed.

Insurance Components

- Health, dental, and life insurance, accidental death and dismemberment, as well as long- and short-term disability insurance.
- The latest summary plan description of anything that has changed since the most recent period of open enrollment.
- The employer's offer to pay for the employee's health and dental coverage under COBRA. Normally an employee can remain on COBRA for 18 to 36 months.

Company Property: Intellectual and Tangible

- Company car, credit cards, keys, laptop, fax, beeper, PDA, and cell phone.
- Customer lists, expense reports, and proprietary information.

Post-termination Services

- Letters or statements of recommendation for a former employee.
- The former employee's use of the company's voicemail for a specified period.
- Length and extent of outplacement services for a former employee.

Post-termination Obligations

- The former employee's obligations under any noncompete, nondisparagement, nondisclosure, or confidentiality agreements he may have signed when he began working there.
- If the employer wants the former employee to sign any added agreements, the employer should recommend that the former employee have them reviewed by an employment law attorney.

❖ What should a Severance Agreement not include?

The Severance Agreement may not prohibit the employee from filing a case of discrimination with the EEOC or local state agency. But it can prohibit the employee from collecting damages if the EEOC files suit against the employer on the employee's behalf.

❖ Does an employer have to provide severance pay?

No. An employer has no obligation to provide severance pay. By law, the only benefit the employer must provide is unemployment compensation.

❖ What does an employer get in exchange for giving an employee a severance package?

The employer gets whatever he writes into the severance plan. Usually, it requires that the employee release all rights, including any right the employee might have to sue the employer, in exchange for the employee getting severance benefits.

❖ What time periods are involved with offering and accepting a Severance Agreement?

In 1989, Congress decided that employees who are 40 years of age and older need extra protection when employers offer them Severance Agreements. So Congress passed the Older Workers Benefit Protection Act (OWBPA). It says that if an employer wants to get a valid release from an age discrimination claim under federal law,

-- the release the employee gives the employer must be “knowing and voluntary.” To meet that standard, the employer must give the employee 21 days (in some cases 45) to consider the severance offer; and

-- the employer must give the employee the opportunity to reconsider and revoke his acceptance of the Severance Agreement. Neither the employer nor the employee can waive the seven-day revocation period.

Severance Agreements are usually written so the employee cannot receive any benefit or payment until after the revocation period has ended. This helps assure the employer that the employee can no longer change his mind. In addition, the employer must advise the employee in writing that he has the right to consult with an attorney before signing the proposed release.

❖ What types of employees are usually offered a severance package?

If severance packages are offered at all, they are usually offered (1) to an executive who has served the employer well, but who is leaving the company due to a reorganization, or (2) to an executive who may have a legitimate claim against the company, from which the employer wants a valid release of that claim.

❖ What does a typical severance package include?

No Severance Agreement is typical. Factors that affect what the employer offers include the employer's size, industry, financial health, past practices, and geographical region where the employer is located. Often, employers think one week of severance pay is appropriate for each year the employee has worked. Other employers have their own rules of thumb. And if the employee has any leverage to use against the company, he might negotiate a severance package in exchange for not filing a claim.

❖ What constitutes an appropriate Severance Agreement?

To determine whether the Severance Agreement is legally appropriate requires answers to two questions: (1) Does the agreement comply with local, state and federal law? And (2) Does the

agreement take into account the terms of the employment agreement between the employer and employee? Since these are legal questions, you should consult your employment law attorney.

Another way to evaluate whether the Severance Agreement is appropriate is to ask whether you think the agreement is fair in light of the circumstances. If not, either the employer or employee can begin discussions to improve the terms of the agreement from his point of view.

❖ **When can an employee break a Severance Agreement?**

Often, an employee can break a Severance Agreement if the agreement

-- is not reasonable in its scope when waiving the employee's rights to sue;

-- violates the law, such as discrimination laws;

-- is not supported by consideration (some type of payment) other than payment that has already been earned; or

-- were not knowingly and voluntarily signed, without a reasonable amount of time to first consider the consequences and consult an attorney.

If you want to learn whether a specific Severance Agreement can be broken, please consult an employment law attorney. (You're welcome to call me at 908-685-0600.)

❖ **Should you have an employment law attorney review your Severance Agreement?**

Yes, without question. Regardless of whether you are the employer or the employee, only an experienced employment law attorney has the knowledge and training to evaluate the agreement. Your lawyer will review the agreement in light of (1) the many local, state and federal laws, (2) your contractual rights and obligations, and (3) any stock option plans or bonus programs.

How to Terminate an Employee: Document!

Firing an employee is never pleasant. Still, if it's part of your job, you should know how to terminate an employee without ending up in court defending a wrongful termination lawsuit.

The key word in terminating an employee is "document." As a general rule, you cannot document enough. Before you reach the point when firing the employee becomes necessary, make sure you document all problems you have had with the employee. This means you should describe, in detail, all actions and behaviors that led to the employee's discipline. Include the date and time every action took place.

After each incident, make sure you list the action you took to reprimand the employee. Then, notify the employee that you have put the reprimand in his employee file. Also, tell the employee that he must sign the reprimand, showing that he has read it. If the employee refuses to sign the reprimand, document this fact as well and have another supervisor sign that he witnessed the employee's refusal.

An Employee Wants to Negotiate a Severance Agreement: Now What?

Employees often try to negotiate a Severance Agreement, usually out of a sense of pride. If you

can be flexible with any of the terms, that may satisfy the employee so he can walk away with his pride still intact.

Instead of offering more money, consider whether a positive letter of reference might satisfy the negotiating employee. Or, you could offer to pay the employee's first two months of COBRA payments, especially if he has a special health-care need in his family.

If you decide to negotiate, make sure you include the costs of negotiation in your settlement offer. If you are willing to negotiate for an additional amount of money, specify that amount in advance. Then state that once your expenses have reached the maximum amount, you will either stop negotiations with the former employee or reduce the offer so you break even at the end.

Before you sign the final Severance Agreement, ask your employment law attorney to review it.

How to Use a Severance Agreement to Avoid a Lawsuit

At times, you know that firing an employee will be hard and could even result in a lawsuit. Perhaps the employee stirs up trouble in the workplace, or maybe you've made mistakes in managing the employee and don't want a judge or jury to review your decisions.

Whatever the reason, if you worry about the employee filing a wrongful termination claim, you will want to have the employee sign a release, which is an agreement not to sue the company in exchange for certain benefits.

You should consult an employment law attorney to discuss your specific situation and ask him to write a legal agreement that meets your needs. In general, these are things you should consider:

❖ You must give the employee more than he would ordinarily receive.

If you offer all employees a severance package even if they don't sign a release, then you must offer something extra to employees who do sign. Usually, this is a sum of money.

❖ State clearly the rights the employee is waiving.

For example, you might state that the employee waives all rights to sue you for claims arising out of the employment relationship, including the termination of that relationship. In addition, you can include that the employee may not encourage or assist others in filing suit against the company. Bottom line, make sure the release is specific enough to prevent any later claim that the employee didn't know what it covered -- and all-inclusive enough to cover every claim the employee might raise.

❖ Give the employee a reasonable amount of time to sign.

This usually means you should give the employee at least one or two weeks to decide whether to waive his right to sue. Also, suggest that the employee ask a lawyer to review the document.

❖ Avoid any appearance of coercion.

A court will not enforce the release unless the employee's decision to sign the release is voluntary. If you threaten or strong-arm your employees to convince them to sign the release, you can expect the judge to throw the release out of court.

❖ **Pay special attention to employees who are age 40 and older.**

For workers who are 40 years of age or older, a federal law -- the Older Workers Benefits Protection Act (OWBPA) -- dictates what you must include in the release. Among other terms, you must give older workers 21 days to review the release and seven more days to revoke the agreement if they change their minds. Also, you must advise them in writing to consult a lawyer.

7 Costly Mistakes to Avoid Regarding Severance Agreements

Costly Mistake #1: Failing to use a current Severance Agreement. Employment laws can be changed by legislatures -- and what they mean can be interpreted by courts. As a result, a Severance Agreement written for a new hire last year may expose you to legal liability if you use the same agreement for a new employee this year. Don't risk using an old agreement. Call me and let me make sure your Severance Agreement is up to date.

Costly Mistake #2: Assuming the law has stayed the same. Employment laws exist at the local, state and federal level. Even if you try to stay current on local laws, new state or federal laws can land you in court. It's not worth the risk, cost, hassles or legal fees. Call me and let me make sure what you want to do today is legal today.

Costly Mistake #3: Relying on this guide to draft your own Severance Agreement. I wrote and published this simplified guide as an educational tool to help you understand the many issues related to Severance Agreements. This guide does not cover all the issues. What's more, the law may have changed since I published this guide. Call me and I'll make sure you have the information you need in your Severance Agreement.

Costly Mistake #4: Failing to call an employment law attorney. The law is highly specialized and most attorneys don't stay current on employment law issues. You wouldn't call a personal injury lawyer when you need a bankruptcy lawyer. Likewise, don't call a bankruptcy lawyer when you need an employment law attorney.

Costly Mistake #5: Assuming you know the answers to employment law questions. Unless you are an employment law attorney -- and unless you stay current on employment laws and decisions -- you won't likely know the answers to today's complex employment law questions. Even employment law attorneys need to check the latest statutes and read the latest decisions to give you competent legal advice.

Costly Mistake #6: Assuming the area of employment law is clearly defined. Employment law overlaps with many other practice areas including contract law, insurance law, benefits law, tax law, intellectual property law, federal law, and more. Your employment law attorney must have knowledge, skill and experience in all these areas. That's why my 30 years practicing employment law pays off handsomely for my clients.

Costly Mistake #7: Failing to hire an attorney who has extensive experience trying cases in all of the courts where your case might go. Since employment law cases can be tried in both state and federal courts -- and then can be appealed to higher state and federal courts -- you need an employment law attorney who is licensed to practice, and has in-depth experience in, state and federal trial and appellate courts. I do.

MEET FRANKLYN C. STEINBERG, III



Mr. Steinberg is the founder and principal of Steinberg Law, LLC. He has practiced law in New Jersey for 32 years.

Practice Areas: Mr. Steinberg represents clients in matters relating to Professional Practices; Business Formation, Purchases and Sales; Commercial Litigation; Employment Law and Litigation; Aviation Law; Sports Law; General Business Law; and state and federal trials and appeals.

Legal Experience: Mr. Steinberg began his legal career as a law clerk to the Hon. Frederick B. Lacey, one of the most distinguished trial judges of the United States District Court for the District of New Jersey. He received his early training as a trial lawyer at a prestigious New Jersey law firm. After achieving partnership status at another established New Jersey firm, he decided to put his experience to work in his own law practice.

Education: In 1974, Mr. Steinberg graduated *magna cum laude* from Denison University (Granville, Ohio). And in 1977, he received his law degree from Seton Hall University School of Law (Newark, New Jersey), where he also served as Managing Editor of the Seton Hall Legislative Bureau.

Trial Experience: Over the past 32 years, Mr. Steinberg has litigated hundreds of complex matters before the State and Federal courts. His extensive trial experience spans a wide range of cases. He has litigated both jury and non-jury trials and has argued appellate matters in the U.S. Third Federal Circuit Court of Appeals, the Superior Court of New Jersey, Appellate Division, and the Supreme Court of New Jersey. Mr. Steinberg serves as local counsel for out-of-state firms in federal litigations. Also, he frequently represents clients in mediation and arbitration proceedings.

Court Admissions & Professional Memberships: He is admitted to practice before the Supreme Court of New Jersey (1977), the United States District Court for the District of New Jersey (1977) and the United States Court of Appeals for the Third Circuit (1978). Mr. Steinberg is a member of the American Association for Justice, the Mid-Atlantic Aviation Coalition, the Lawyer-Pilot's Bar Association and the Aircraft Owner's and Pilot's Association.

Employment Law: In addition to litigation, a significant area of focus for Mr. Steinberg is employment law. He often represents executives and individuals in employment disputes involving *Fortune 500* companies. Many of these matters have been resolved through his successful negotiation of separation agreements that provided for substantial compensation packages.

Aviation Law: An avid pilot for more than 30 years who holds a commercial license, Mr. Steinberg also actively practices in the area of aviation law. He also counsels the Firm's business clients.

Civic Service: For the past 20 years, Mr. Steinberg has been involved in the Somerset County Business Partnership. This year he serves as Chair of its Board of Directors. In addition, Mr. Steinberg teaches Sports Law in Seton Hall University's Stillman School of Business. He has been a featured speaker for the New Jersey Institute for Continuing Legal Education and various professional groups.

You're Invited to Call or E-mail.

"If you have questions about any aspect of business law, commercial litigation, employment law, aviation law, sports law, or state or federal trials and appeals -- please don't hesitate to call. I'll be happy to help you in every way!" -- *Frank*

FRANK STEINBERG BUSINESS & TRIAL LAWYER

*Helping Entrepreneurs and Professionals
Solve Problems ... Reduce Risk ... Seize Opportunities ... Increase Profits*

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"Frank gave one of my clients sound, practical advice, including not pursuing litigation."

I've known Frank for 30 years. He's a gentleman and a delight to work with -- and he has a great sense of humor. I had a situation where one of my accounting clients made a mistake. Frank helped negotiate a good resolution and gave sound, practical advice, including not pursuing litigation because the upside wasn't there. Frank is my tax client and I am Frank's corporate client. I have referred clients and colleagues to Frank -- and will continue to refer in the future.

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