

Legislature halts double-dipping

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When Hensley & Company, a Phoenix beverage distributor, implemented a reduction in force (RIF) in 2011, it offered severance to the affected employees based on their length of service. When longtime employee Mark Wynn filed a claim for unemployment benefits despite his receipt of a year's base pay as severance, Hensley fought the claim all the way to the Arizona Court of Appeals and lost. Unhappy with that result, the Arizona Legislature passed a law that will prevent such double-dipping in the future.

Release for a price

When Hensley implemented its RIF, it decided to pay all laid-off employees two weeks of base pay and whatever benefits remained in the month of termination. Employees who would sign a broad release of all claims against the company, known and unknown, would receive a sweeter deal based on their length of service.

Longtime employees such as Wynn, who had worked at Hensley for 33 years, would get a full year's base pay in exchange for signing the release. Hensley offered lower severance payments to employees with less tenure, with a minimum of three months' base pay for employees with fewer than 15 years of service who would sign the release. The severance amounts the company offered were nonnegotiable.

Wynn accepted his \$75,600 payment in November 2011 and then filed a claim for unemployment benefits in December 2011. The Arizona Department of Economic Security (ADES) initially denied his claim based on the lump-sum severance payment. The initial ADES decision was based on A.R.S. § 23-621, adopted by the legislature in 2004 in an attempt to prevent unemployed individuals from drawing state benefits while "receiving wages in lieu of notice, dismissal pay or severance pay." The statute deemed folks not unemployed for the number of workdays the severance payment would cover at their regular pay rate.

Wynn appealed, and an administrative law judge (ALJ) concluded that 50 of the 52 weeks of base pay he received was consideration (i.e., payment) for the release, making him eligible for unemployment benefits when he initially applied in December 2011. Hensley was not happy with the ALJ's ruling and appealed to the ADES Appeals Board, which ruled the entire amount, all 52 weeks, was severance pay, making Wynn ineligible for benefits for a year.

Wynn's win

Wynn appealed to the Arizona Court of Appeals, and on January 7, 2014, the court ruled in his favor. According to the court of appeals, whether the payment was truly severance pay or was instead a payment to obtain the release depended on five relevant factors:

1. The employer's motivation to assist the employee in searching for new employment;
2. The language used in the agreement and by the parties to describe the payment;
3. The breadth of the release;
4. What, if anything, the employee would receive if he refused to sign the release; and
5. Whether the employee has any claims to waive.

The court found that Hensley's motivation to assist employees financially extended only to the two weeks of wages everyone received. Although both parties and the agreement called the payment "severance," the court regarded that factor as neutral. The breadth of the release was a factor counted against Hensley, as was the relatively small severance payment available to Wynn if he refused to sign the release.

Finally, even though Wynn testified at his unemployment appeal hearing that he had no claims against Hensley to release, the court determined that the inclusion in the release of unknown claims and any claims he might be releasing through "ignorance, oversight, error, negligence, or otherwise" was a factor weighing against the company.

The court of appeals ultimately ruled that the ALJ was correct and that only two weeks' worth of the payment to Wynn was severance. That meant he was disqualified from unemployment benefits for only the first two weeks after the layoff.

Legislative fix

Within a few weeks after the court of appeals' ruling, Representative Karen Fann (R-Prescott) introduced a bill designed to require a different outcome in similar cases in the future. The bill adds a new section to A.R.S. § 23-621 defining severance pay, a term not defined by the 2004 legislation, to include "all amounts that an employer pays to an employee due to the employee's resignation, termination or participation in an exit incentive program or inclusion in a reduction in force or in consideration for the employee's release of actual or potential claims for the termination of employment."

The bill passed the Arizona House and Senate and was signed by Governor Jan Brewer on April 24, 2014. The new law will take effect on July 24, 2014.

According to Representative Fann, quick action was needed to clarify the law and eliminate the double-dipping allowed by the court of appeals' decision to protect the solvency of the state's unemployment trust fund. That fund is financed by the tax that employers pay on the first \$7,000 of each worker's salary. During the Great Recession, the fund went broke, and Arizona had to borrow money from the federal government.

Bottom line

When the new law becomes effective, Arizona employers can rest assured that former employees to whom they pay severance won't be drawing unemployment benefits right away. Those former employees will not even be considered unemployed until the workdays the severance pay would cover at their base pay rate are exhausted.

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