

U.S. Department of Labor

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



August 27, 1996

96-16A
ERISA SEC. 3(1)

Mr. Scott J. Morris
Assistant General Counsel
Northwestern Mutual Life
720 East Wisconsin Avenue
Milwaukee, Wisconsin 53202-4797

Dear Mr. Morris:

This responds to your request for an advisory opinion that the NML Employee Disability Income Plan (Plan) is an employee welfare benefit plan within the meaning of section 3(1) of the Employee Retirement Income Security Act of 1974 (ERISA).

Your submission contains the following facts and representations. The Northwestern Mutual Life Insurance Company (Company) maintains the Plan to provide benefits to all regular full-time and part-time employees who are unable to work due to illness or injury.¹ The Plan specifies that benefits are provided according to three phases, as follows:

Phase I. After an employee is absent from work for five consecutive workdays due to disability, the employee is entitled to a wage continuation benefit equal to 100% of compensation for each workday of absence. The total benefit amount is limited to the greater of ten days' compensation or five days' compensation for each year of service with the Company.

Phase II. After the expiration of Phase I benefits, an employee is entitled to 70% of compensation until the earlier of the date the employee recovers from the disability or the expiration of one year from the commencement of the disability.

Phase III. If the disability continues beyond one year, the employee becomes entitled to long-term disability benefits equal to 70% of annual compensation up to \$20,000 and 60% of annual compensation in excess of \$20,000. The employee is also entitled to a cost-of-living adjustment, before certain benefit reductions described below, as calculated under the Northwestern Mutual Retirement Plan (Retirement Plan). Phase III benefits are paid monthly and continue until the earliest of (a) the employee's recovery from disability, (b) the end of the "maximum benefit period," or (c) the employee's death. The Plan's provisions specify that the maximum benefit period is determined by the employee's age when the disability begins. If disabled at age 61 or younger, the maximum benefit period runs to age 65, or 3 years 6 months, if longer. For employees disabled at age 62 or older, the maximum benefit period is scaled downward from 3 years 6 months to a period of one year in the case of employees disabled at age 69 or older.

The Plan specifies that benefits under Phases I, II, and III are to be reduced by any amount the employee or any dependent of the employee receives under certain other programs, including Social Security and the Retirement Plan. In addition, if the employee reaches his or her normal retirement date and does not elect to retire, Phase III

¹ Certain other employees, described as "long-term temporary" and "long-term accommodation" employees, are eligible for Phase I benefits only. These employees comprise approximately two percent of all plan participants.

benefits are offset by the amount that the individual would receive as a normal retirement annuity under the Retirement Plan, if he or she had elected to retire.

The Plan further provides that an employee who is receiving Phase I or II benefits and has not elected to retire under the Retirement Plan is deemed an employee of the Company for purposes of all fringe benefits, including vacation credits and seniority. An employee who is receiving Phase III benefits and has not elected to retire under the Retirement Plan ceases to be considered an employee for any purpose except accrual of benefits under the Retirement Plan and participation in the Company's group life insurance and flexible benefit plans. The Plan indicates that employees who are receiving any benefits under the Plan and have elected retirement are no longer considered employees of the Company for any purpose.²

You represent that the Plan is unfunded and all benefits are paid out of the general assets of the Company. The Plan specifies, however, that the Company retains discretion to pay benefits through a group disability income insurance policy, a trust, separate account or any other lawful means.

For the reasons that follow, it is the opinion of the Department of Labor (Department) that the Plan is an employee welfare benefit plan within the meaning of section 3(1) of ERISA.

Section 3(1) of ERISA defines the term "employee welfare benefit plan" to include, as relevant here, any plan or program established or maintained by an employer to provide to its employees benefits in the event of sickness, accident, or disability. The Department clarified the scope of section 3(1) in regulations that, among other things, identify certain employer payroll practices that are not included within this definition. Specifically, as relevant here, regulation section 29 CFR 2510.3-1(b)(2) describes the following employer practice as excluded from the meaning of "employee welfare benefit plan:"

Payment of an employee's normal compensation, out of the employer's general assets, on account of periods of time during which the employee is physically or mentally unable to perform his or her duties, or is otherwise absent for medical reasons (such as pregnancy, a physical examination or psychiatric treatment)

The information furnished indicates that the Plan is clearly an employee welfare benefit plan as defined in section 3(1) of ERISA, unless the Plan is excluded from that definition as a payroll practice described in regulation section 2510.3-1(b)(2). On the basis of the information furnished, it is the view of the Department that the Plan is not a payroll practice within the meaning of that regulation.

In the preamble of the regulation, the Department stated that "[s]ection 2510.3-1(b) distinguishes welfare plans from employer payroll practices which, although related to benefits described in [section 3(1) of ERISA], are more closely associated with normal wages or salary," and that "[p]aragraphs b(2) and b(3) of §2510.3-1 are designed to deal with payment of compensation out of general assets of the employer during periods of employee absences." 40 Fed. Reg. 34526 (August 15, 1975) (emphasis added). It is thus evident that the "sick pay" exclusion is intended to apply to arrangements in which compensation continues to be paid to individuals who are absent from service, but who remain employees during the periods for which their compensation continues to be paid. This payroll practice exception is not intended to apply to arrangements that continue cash payments to individuals, in amounts related to the individuals' prior compensation for services, after the individuals have ceased to be considered employees, such as when they resign or retire. Under any of the three Phases of the Plan, benefits may be paid to individuals who have elected retirement and are no longer considered to be employees of the Company. In addition, recipients of

² See section 4, Art. VI. of the Plan together with sections 1, 2, and 3, Art. VI. of the Plan.

Phase III benefits who have not elected retirement are considered employees only for the limited purpose of coverage under certain benefit plans.

We note as further indication that the Plan is not an arrangement contemplated by regulation section 2510.3-1(b)(2) that the benefit amount paid under Phase III includes a cost-of-living adjustment that is calculated under the terms of the Retirement Plan and the benefit amount is offset by the amount of the normal retirement annuity that would be payable upon reaching normal retirement eligibility, even though the benefit recipient does not elect retirement. A sick pay plan that determines benefits in part on the basis of the benefit provisions of the employer's retirement plan and by treating the benefit recipient as if he had elected retirement, when in fact the recipient has not so elected, does not, in the view of the Department, provide "normal compensation" within the meaning of the sick pay regulation.

You also expressed concern that the Plan should be considered a single employee welfare benefit plan, rather than several plans in which Phase I and/or II benefits would be separately classified as payroll practices while Phase III benefits are treated as an ERISA-covered plan. In this regard, it has been the position of the Department that whether there is a single plan or multiple plans is an inherently factual question on which the Department ordinarily will not opine in the advisory opinion process. See section 5.01 of ERISA Procedure 76-1 (41 Fed. Reg. 36281, August 27, 1976). We note, however, that the information you submitted does not include anything that would necessarily indicate that the Plan is other than a single welfare benefit plan under ERISA.

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

Sincerely,

Susan G. Lahne
Chief, Division of Coverage
Office of Regulations and Interpretations