Unique Severance Program Offers Big Benefits to All Companies During Lay-Offs

In recent years, the economic downturn has led to widespread involuntary reductions in workforces across many diverse industries. Because these staff reductions are costly, Fortune 1000 companies have struggled to control severance costs while providing reasonable severance benefits at the same time. Consequently, there has been renewed interest among large companies in an alternative severance program known as a Supplemental Unemployment Benefit ("SUB-Pay") Plan.

SUB-Pay Plans allow employers to offset the total cost of their severance obligation by amounts payable under state unemployment insurance ("UI") benefits. For over 50 years SUB-Pay Plans have helped many major U.S. companies save 7.65%-45% in severance costs from payroll tax savings and the coordination of state UI benefits. Also, because SUB-Pay must be made on a periodic basis, there was predictability to the process that was beneficial to the company's cash flow.

SUB-Pay Plans can be right-sized for any company

While used by larger companies, today, the application of SUB-Pay Plans has entered the mid- and small-cap markets as well, and is relevant in multiple lay-off contexts such as M&A and business realignment scenarios. When properly structured, these plans can yield significant tax and financial advantages to any employer and their separated employees.
Although the savings from SUB-Pay Plans are based on a number of factors including plan design and the amount and deration of individual state UI benefits, implementation is not as complex as it may seem. Additionally, the threshold for qualification is within reach:

- The SUB-Pay Plan must be in writing;
- Separated employees must be eligible for state UI benefits in order to receive SUB-Pay benefits. Plus, they must update their ongoing eligibility for state UI benefits;
- SUB-Pay benefits must be made on a periodic basis and cannot be made in form of a lump sum;
- SUB-Pay plans must comply with IRS regulations as well as federal and state laws.

Sizing up the benefits of SUB-Pay

Company Benefits

A SUB-Pay Plan can save a company 7.65 percent in severance costs from FICA payroll tax savings on the separation payments, as well as federal and state unemployment tax savings of about 3 percent or more, depending upon the state, the employer's experience rating, and the time of year that the reduction in force occurs.

A SUB-Pay plan also can save a company 35 to 45 percent of their total severance costs by supplementing the separation payments with state UI benefits the former employees are eligible to receive. For example, if an employee's pre-layoff wage was $1,000 a week and the state UI benefit is $500 a week, the company pays only $500 a week in separation pay to keep the employee at the pre-layoff wage and saves 7.65 percent in FICA tax. Essentially, a lay-off of 175 employees could save a company up to $750,000 in severance payment costs.

And, as is the case with any company, no matter their size, the benefits are paid on a periodic basis, reducing the cash flow impact to the company. Finally, once a SUB-Pay Plan is established it can continue to be used indefinitely for any involuntary staff reductions.

Employee Benefits

There are a number of significant benefits to the employee as well. The separated employees receive 7.65 percent more net income and get a regular income for the duration of their separation plan. Contrast this with lump-sum severance payments that are taxed at a higher rate than wages paid on a periodic basis, and when added to an employee's year-to-date compensation, may elevate the employee into a higher tax bracket. Because SUB-Pay Plans are paid on a periodic basis, the former employee is provided with steady income during their reemployment transition, and may be relieved of the additional tax burden associated with lump-sum severance payments.

No pain, all gain when you outsource plan administration

While some employers create and administer SUB-Pay Plans in-house, outsourcing SUB-Pay administration to a reputable company can significantly alleviate the additional work and stress layoffs can bring to HR and payroll departments. A dedicated SUB-Pay Plan partner will assist in ensuring the Plan is compliant with IRS rulings at the federal level, and that the Plan is in compliance at the state level. In addition, a dedicated plan partner provides laid-off workers with a ready resource to help them during their transition period including individual call center assistance plus, IVR and web support services. Finally, another added benefit is that an outsourced provider can serve as an "advocate" to separated employees who may need help with opening their state UI claims or resolving other issues that may come up.

A good fit for companies regardless of size

Whether a large or small company, SUB-Pay Plans can create a win-win situation for companies and separated employees during a lay-off period. And outsourcing the process has advantages as well. The overall benefits are difficult to ignore:

- Ability to pay "severance" benefits to former employees without impacting their eligibility for, or amount of, state UI benefits;
- To reduce FICA and FUTA taxes otherwise payable in typical severance arrangements (resulting in a savings to the company and former employee of up to 7.65 percent each); and,
- To efficiently use payroll taxes already provided to the state for UI benefits (in certain plan designs) resulting in company savings of up to 45 percent.