Protection For The Non-Innocent

ERISA Protection Regulations Are So Tight That They Can Protect an Employee Who Embezzles

By Peter R. Spanos, Esq.

Nicholas Vink was convicted of defrauding his employer, Geveke & Co. International, Inc.

He pleaded guilty to having received an illegal $25,000 kickback and bribe from a customer and supplier and having falsely represented on a bank application that Geveke & Co.’s board of directors had agreed to guarantee repayment of a $95,000 personal loan sought by Vink. In addition, he allegedly received many thousands of dollars in other kickbacks and embezzled more than $3,000,000 from his employer.

Mr. Vink was sentenced to 14 months imprisonment for his misconduct.

Despite his conviction and prison sentence, the unrepentant Vink submitted a claim for his vested benefits under his former employer’s ERISA-qualified profit sharing plan, which the plan’s trustee quite naturally denied. Mr. Vink, however, was not to be denied and took his claim for payment of vested profit sharing benefits to federal district court. Incredibly enough, he won! Vink v. SHV North America Holding Corp., 549 F. Supp. 268 (S.D. N.Y. 1982).

In pre-ERISA days, there would have been no question that a company could deny pension or profit sharing benefits to an employee who had defrauded it and embezzled its funds. So-called “bad boy” clauses, which provided for the forfeiture of pension benefits in the event of employee misconduct, were common provisions in pension plans before the enactment of ERISA.

Unfortunately, many of those clauses were extremely broad, denying benefits not only to an employee who cheated the employer or stole trade secrets, but also to a “disloyal employee” who went into competition with the employer after retirement or who simply said bad things about his former employer.

Because of a widespread abuse of “bad boy” forfeitures, Congress effectively eliminated all forfeiture of qualified plan benefits for misconduct in ERISA. ERISA allows forfeiture of vested benefits only in four specific circumstances, none of which involves employee misconduct.

So, for example, an ERISA-qualified plan can be drafted in a manner that it denies payment of vested benefits to the estate or surviving spouse of a faithful 30-year employee who dies one day before reaching the plan’s retirement age, but the plan cannot withhold the vested benefits of an embezzler who survives to the plan’s retirement age.

Supporting ERISA’s non-forfeiture provisions are its provisions prohibiting assignment or alienation of benefits. The Internal Revenue Service Regulations issued pursuant to this portion of ERISA state that “benefits provided under the plan may not be . . . assigned . . . alienated or subject to attachment, garnishment, levy, execution, or other legal or equitable process.”

In the Vink case, the Court pointed out that, together, “these provisions prohibit both the voluntary and involuntary assignment of vested pensions . . . . It is unclear,” the Court continued, “whether [the former employer] in refusing to make pension
payments to Vink has employed a species of forfeiture or of involuntary assignment of Vink’s benefits back to the pension fund.

Whichever the case may be, ERISA’s non-forfeitability and non-assignability provisions clearly cover it.” Thus, the non-assignability provisions of ERISA make vested pension benefits, while still in the hands of the plan trustees, virtually judgment-proof.

Even if the employer obtains a judgment against an embezzler, it cannot enforce that judgment by attachment or garnishment of the embezzler’s vested benefits in the hands of the plan trustees.

The employer in the Vink case argued that public policy should imply a fraud exception to the non-forfeitability rules, just as courts have previously determined that public policy implies an exception to the non-forfeitability and non-assignability rules for the purpose of allowing divorced and separated spouses of a plan participant to enforce support judgments against vested plan benefits in the hands of the plan trustees.

The Court in Vink did not deny the merit of the employer’s argument, but rejected it because “there is an unambiguous declaration of intent by Congress to prevent the enforcement of “bad boy” clauses.” The Court commented that if ever there were a case to carve out a fraud exception to the non-forfeitability rules, Vink would seem to be it. Not only did the embezzler cheat his employer, his actions, by reducing overall company profits, also subtracted from the amounts the employer’s faithful employees would receive from the company’s profit sharing plan. Thus, the dishonest employee, whose benefits are nonforfeitable, causes constructive forfeitures of part of the benefits of the honest employees.

The Court found this “most dismaying,” but repeated that Congress
has made the law clear—pension benefits of dishonest employees are to be protected even if it means that faithful employees will suffer as result!

Unless and until the non-forfeitability provisions of ERISA are changed to deal with cases such as Vink, employers may consider another course of action to prevent an embezzling employee’s receipt of vested plan benefits. Employers should consider amending their qualified plans to provide: (1) that benefits will be paid in a lump sum or as an annuity, at the option of the employer; and, (2) that benefits will be paid or will commence upon separation from service or at normal retirement age except that, if the employee is involved in litigation with the employer, distribution will be delayed until the lawsuit is settled.

When the embezzling employee is fired, the company can simultaneously commence a civil action against him for the amount he stole. His claim for pension benefits can be honored with a lump sum payment after the company obtains a judgment in its lawsuit. Then as soon thereafter as possible, the company can have the judgment enforced and recover the lump sum payment.

(Editor’s Note: Peter R. Spanos is a well-known construction attorney and a principal in the law firm of Summers, Hendrick, Spanos & Phillips, of Atlanta, GA. This article was taken from the firm’s construction newsletter.)