

DEPARTMENTAL GRANT APPEALS BOARD

Department of Health and Human Services

SUBJECT: Alcoholism Center for Women  
Docket No. 81-49  
Decision No. 222

DATE: October 29, 1981

DECISION

By letter dated March 23, 1981 the Alcoholism Center for Women (Grantee) appealed a decision of the Alcohol, Drug Abuse, and Mental Health Administration Grant Appeals Committee (Agency), upholding the disallowance of a \$9,166.92 charge to Grant No. H84-AA-02893 for severance pay to Grantee's former Executive Director.

Our decision is based upon Grantee's application for review, the Agency response, relevant documents submitted by both parties, an Order to Show Cause issued by the Board on August 26, 1981, and the parties' responses to that Order.

Background

Grantee's Executive Director resigned by letter submitted to Grantee's Board of Directors at a September 21, 1977 meeting. The Board of Directors accepted the resignation and decided to grant the former Director six months salary as "severance pay." The facts indicate that the Director's resignation was voluntary and the minutes of the meeting state simply that "the topic of severance pay was discussed." Congratulatory remarks were addressed to the Director in recognition of her past service, but no other justification for the award in question can be discerned from the minutes. In January 1978, the Executive Director was paid \$10,000.28, as severance pay, and that amount was charged to the grant.

In June 1980, the National Institute on Alcohol Abuse and Alcoholism (NIAAA) conducted a site visit to Grantee in which it received documentation to show that the award of severance pay was broken down in the following manner: \$6,666.92 as 4 months salary and \$3,333.36 as 2 months accrued leave (Site Report, p. 2). NIAAA determined that the payment to the former Director was inappropriate because it was contrary to the Grantee's established personnel policy. The entire amount of severance pay classified as salary, as well as \$2,500 in accrued leave, was disallowed.

Grantee appealed the disallowance to the Agency, contending that the award of severance pay was made in accordance with the cost principles, 45 CFR Part 74, Appendix F, G.40.

Grantee asserted that the payment was the result of an employer-employee agreement; that the award was made in accordance with an established policy of Grantee; and that it was called for by circumstance of the particular employment. Further, Grantee claimed that a November 15, 1977 letter from its Assistant Director to the Program Administrator (Special Projects Branch, Western Section), NIAAA, served as timely and constructive good faith notice of Grantee's intention regarding the severance pay.

Based upon the grounds that Grantee's actions in awarding severance pay violated controlling cost principles, the Agency upheld the disallowance. The Agency also found that Grantee's letter to NIAAA did not constitute prior notice of the intended charge to the grant.

By letter dated June 3, 1981 (Letter), Grantee informed the Board of the discovery of "a material bookkeeping error." Grantee advised the Board that the entire amount of severance pay was properly classifiable as salary. As noted earlier, the Agency thought the award of severance pay included \$3,333.36 in accrued leave, \$2,500 of which was disallowed, apparently providing Grantee with \$833.36 in costs chargeable to the grant. Since the disallowance before the Board is limited to \$9,166.92 (\$10,000.28 - \$833.36), our decision will address that amount only.

#### Discussion

The regulation at 45 CFR Part 74, Appendix F, G.40. Severance Pay, provides:

- (a) Severance pay, also commonly referred to as dismissal wages, is a payment in addition to regular salaries and wages, by institutions to workers whose employment is being terminated. Costs of severance pay are allowable only to the extent that, in each case, it is required by (1) law, (2) employer-employee agreement, (3) established policy that constitutes, in effect, an implied agreement on the institution's part, or (4) circumstance of the particular employment.

Grantee does not contend that the severance pay in this case was required by law, but seeks to demonstrate that it meets one of the three remaining regulatory conditions. 1/

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1/ In our Order we questioned whether the regulation applies to those situations where an employee receives a bonus for meritorious work upon voluntary resignation since the pay at issue would not be "severance pay" within the ordinary meaning. We do not reach that issue in our decision, however, since the Agency has acquiesced in the application of the "severance pay" regulations to the circumstances here.

Employer-Employee Agreement

Grantee has stated that to the best of its knowledge a written employment contract between itself and its Executive Director did not exist. Grantee claims, however, that "a contract (oral and/or implied) obviously existed, or was understood ... and was subject to modification especially if by mutual agreement" (Letter, p. 1). It is Grantee's contention that such a modification occurred when its Board of Directors voted to make an award of severance pay. Grantee argues that its actions "represented a mutually accepted condition of employment, even to the extent of the obvious termination of such employment and the retroactive nature of the decision" (Letter, p. 2).

Grantee's argument lacks merit in several respects. Grantee admits that no written agreement exists. Further, even if an "oral" agreement were sufficient, Grantee has presented no evidence of the terms of such an agreement, nor has Grantee demonstrated that such an agreement was entered into prior to, or at the inception of employment. By arguing that Grantee's Board of Directors met the agreement condition by modifying an implied contract following the Director's resignation, Grantee is stripping the regulation of any substance.

The element central to the allowability of severance pay is that it must be "required" by an agreement. Grantee does not claim that severance pay was an originally agreed upon condition of a contract with its Executive Director. Had an original employment agreement required severance pay there would be no need to "modify" it. The "modification" occurred after the Executive Director's resignation. She did not forego a right to finish out a defined term of employment in exchange for severance pay; she resigned of her own volition.

Given the above facts, it is the decision of the Board that severance pay was not required by an employer-employee agreement in this case.

Established Policy

Grantee claims that the decision of its Board of Directors to award severance pay, was made pursuant to an established policy.

Again, Grantee has applied a reading of the regulation which is broader than reasonable. Grantee has included in the case file excerpts from its relevant personnel policy. Under this policy Grantee did not provide severance pay for voluntary terminations. It apparently did allow for two weeks severance pay, in lieu of two weeks notice, for employees who were terminated for any reason other than engaging in a "prohibited practice." From the facts before us it cannot be said that Grantee had an established policy calling for an award of severance pay to any employee voluntarily resigning. In fact, the silence of the personnel policy on severance pay for employees who

resign is arguably a policy not to award such pay, in view of the explicit provision for severance pay in certain other circumstances.

The action of Grantee's Board did not establish a policy on severance pay. Use of the term "policy" in the cost principles envisions a definite course of action, generally applicable. Grantee has not shown that its decision to award six months severance pay was based upon any preexisting scale or formula. It did not delineate a policy which could be followed, in any definite manner, for other employees in like circumstances. Accordingly, we conclude that the award of severance pay here was not required by an established policy.

#### Circumstance of the Particular Employment

Grantee's argument that there were obviously "circumstances of the particular employment" requiring severance pay or there would have been no need for the actions of its Board of Directors is circular at best. Grantee in effect contends that the very fact that severance pay is not, under the facts of this case, clearly required by law, employer-employee agreement, or established policy is itself a circumstance which requires severance pay.

The regulatory provision allowing severance pay where particular circumstances require it cannot reasonably be viewed as a catchall clause which would allow severance pay when it cannot be justified by any of the other criteria in the regulation. The regulations evidence an intent to establish limits for the allowability of severance pay. Such pay is allowable "only to the extent" that it is required. An appropriate example would be where an institution such as Grantee would be harmed if an incompetent executive director were to remain in that position for a full term. Thus, the element of give and take would exist where Grantee gives severance pay and the employee steps down in advance of a predetermined time. (See Health Systems Agency of Western New York, Inc., Decision No. 221, October 21, 1981.)

Grantee claims that severance pay was justified because this was its first Executive Director and no precedent existed for handling her employment or termination (Letter, p. 2). As noted above, Grantee's personnel policy provided for severance pay only in the context of a non-voluntary termination and then only in lieu of two weeks notice. It is reasonable to assume that Grantee's stated policy was a decision to preclude its award in any instance of voluntary resignation. Thus, Grantee's argument regarding lack of precedent and opportunity to deal with the Executive Director's voluntary termination is not persuasive.

As noted above, the minutes of the Board of Directors meeting provide no indication of any circumstances which compelled the Directors to award severance pay to the Executive Director. Further, we find it

hard to conceive of circumstances in which voluntary resignation would require six months salary as severance pay. Essential to the allow-ability of any cost is the element of reasonableness. The extent of pay allowable under "circumstance of the particular employment" must necessarily be determined by that circumstance and limited by general principles of reasonableness. The excessive nature of the award here is further reason for us to conclude that it was not required by the circumstance of the particular employment.

Notice

Grantee asserts that the November 15, 1977 letter from its Assistant Director to NIAAA put the Agency on notice of Grantee's intention regarding severance pay and the Director's termination. While no mention of the termination or severance pay was made in the letter itself, a copy of the September 21, 1977 Board of Directors' Minutes was enclosed. Although these minutes effectively notified the Agency of the Director's resignation, no reference was made to the amount of severance pay (other than six months salary) nor that the source would be Federal funds. Hence, Grantee cannot reasonably argue that this letter put the Agency on notice regarding its actions. Moreover, even if the Agency had been on notice, Grantee would still be bound to show that severance pay was required by one of the criteria discussed above, or that such notice would otherwise require the Agency to consider the costs allowable.

Grantee's response to the Order to Show Cause disagrees with the Board's tentative opinions but accepts our presentation of the facts of this appeal. While Grantee maintains that severance pay was proper here as a result of an employer-employee agreement, established policy and the circumstance of employment, Grantee has not offered any new evidence which would compel the Board to alter its preliminary analysis.

Conclusion

For the reasons stated above, this appeal is denied.

/s/ Norval D. (John) Settle

/s/ Cecilia Sparks Ford

/s/ Donald F. Garrett, Panel Chair