PROSKAUER ROSE LLP

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Editor's Overview

This month has no end-of-term flurry of opinions issued by the Supreme Court. The lower courts have, however, issued several decisions of interest, two of which are reported on here. In *Hirt v. Equitable* the Second Circuit joins the Seventh, Third, and Sixth Circuits in holding that the formulas in cash balance plans do not violate the age discrimination prohibitions in ERISA. Like the other circuit courts, the Second Circuit concluded ERISA does not make the consequences flowing from the application of the time value of money unlawful. Whether this is the final end to this claim (which became all the rage for awhile) remains to be seen.

In *Srgo v. Danone Waters* the Ninth Circuit addressed whether a California insurance regulation that required reimbursement of a claimant's cost to copy medical records was saved from ERISA preemption. In applying the *Kentucky Association v. Miller* test, the Ninth Circuit concluded this regulation did not substantially impact the risk pooling arrangement between the insured and the insurer, and thus was not "saved" from ERISA's preemption provisions.

There are also several opinions briefly noted in the final "Rulings, Filings and Settlements of Interest" section, including interesting rulings in the areas of employer stock claims and an ERISA Section 510 claim. Finally, although off the "litigation-beat", and thus not discussed below, the Department of Labor's proposed regulation on fiduciary disclosures in participant-directed individual account plans, issued on July 23, 2008 at 73 Fed. Reg. 43014, will likely impact certain of the claims currently being made in the 401(k) fee-and-expense litigation. The Department's proposed regulation rejects the notion that fiduciaries must disclose revenue-sharing information to participants, instead detailing why it is advantageous to offer participants concise, useful, comparative information. In furtherance of this goal, the regulation proffers as a model a disclosure chart that focuses on providing participants comparative, concise information on the performance and the *total* fees and expense information of the various investment options offered by a plan.

Second Circuit Rules That Cash Balance Plans Are Not Inherently Age Discriminatory

By Myron D. Rumeld and Russell L. Hirschhorn

On July 9, 2008, the U.S. Court of Appeals for the Second Circuit ruled in two parallel appeals that cash balance pension plans do not violate the age discrimination prohibitions of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), Section 204(b)(1)(H), 29 U.S.C. § 1054(b)(1)(H). *See Hirt v. The Equitable Retirement Plan for Employees, Managers and Agents*, No. 06-4757 & *Bryerton v. Verizon Communications, Inc.*, No. 07-1680, 2008 WL 2669346 (2d Cir. July 9, 2008). The ruling, which resolved a split among district court decisions in the Second Circuit, follows the holdings of the Third, Sixth and Seventh Circuits — the only other Circuit Courts to have addressed the issue.

Section 204(b)(1)(H) provides that "a defined benefit plan shall be treated as not satisfying the requirements of this paragraph if, under the plan, an employee's benefit accrual is ceased, or the rate of an employee's benefit accrual is reduced, because of the attainment of any age." In numerous lawsuits challenging the validity of cash balance plans, participants have contended that these plans violate Section 204(b)(1)(H) because the dollar amount of the pension accumulated by older employees at the time they reach their retirement age is less than the dollar amount accumulated by younger employees with comparable years of service. The seeming discrepancy is merely a function of the time value of money: cash balance accruals earned as of a younger age have more years to accumulate interest before the participant reaches retirement age. The issue applies only retroactively, since the Pension Protection Act of 2006 has insulated cash balance plans from such challenges on a prospective basis.

The Seventh Circuit Court of Appeals was the first Circuit to take the issue on. In *Cooper v. IBM Personal Pension Plan,* 457 F.3d 636 (7th Cir. 2006), the court compared section 204(b)(1)(H), covering defined benefit plans with section 204(b)(2)(A), governing defined contribution plans, providing that such a plan satisfies the requirements if "allocations to the employee's account are not ceased, and the rate at which amounts are allocated to the employee's account is not reduced, because of the attainment of any age." The Seventh Circuit observed that while the rule for defined benefit plans is phrased as prohibitory, and that for defined contribution plans it is permissive, they say the same thing — "the employer can't stop making allocations (or accruals) to the plan or change their rate on account of age." The Third Circuit Court of Appeals and Sixth Circuit Court of Appeals followed the same reasoning in *Register v. PNC Financial Services Group, Inc.*, 477 F.3d 56 (3d Cir. 2007) and *Drutis v. Rand McNally & Co.,* 499 F.3d 608 (6th Cir. 2007).

Like the other Circuits, the Second Circuit rejected arguments that this "discrepancy" constitutes age discrimination under ERISA and concluded that the "rate of benefit accrual" refers to the employer's contribution to a plan. Rejecting plaintiffs' arguments, the Court found there was no reason to equate the term "rate of benefit accrual" with the ERISA defined term, "accrued benefit", which is measured by reference to the end product — the age-65 annuity that can be purchased with the account balance. Thus, as long as contributions to the cash balance account are made on a nondiscriminatory basis, there is no violation of ERISA merely because contributions made for younger participants are worth more at age 65 than contributions made for older participants.

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The Second Circuit ruling makes it quite likely that the age discrimination issue has been put to bed for cash balance plans. Although there is at least one appeal pending in the Ninth Circuit on this same issue, most anticipate that it too will follow the holdings and reasoning of the four Circuit Courts that have unanimously rejected these claims. Should the Ninth Circuit (or any other Circuit) rule to the contrary, however, there might still be a need for Supreme Court resolution. Stay tuned.

Ninth Circuit Gives Meaning to Savings Clause' "Risk Pooling" Requirement, Ruling That California Insurance Regulation Requiring Reimbursement of Copying Costs for Medical Records is Not "Saved" From ERISA Preemption

By Robert Rachal

In *Sgro v. Danone Waters of North America, Inc.*, 2008 WL 258936 (9th Cir. July 2, 2008), plaintiff Mitchell Srgo submitted a disability claim to MetLife. To acquire the materials needed for this submission, Mr. Srgo spent $412 to obtain copies of his medical records from his medical providers. A California insurance regulation required insurers to reimburse claimants for the costs of copying any requested medical records.

The Ninth Circuit concluded that the regulation did not satisfy the two part test enumerated in *Kentucky Association v. Miller*, 538 U.S. 329 (2003), for determining when a regulation affecting insurance is exempted from ERISA preemption under ERISA's "Savings Clause." The court ruled there was no question that the regulation met the first part of the *Miller* test, as the regulation applied only to insurers, and thus was clearly directed toward the insurance industry. The closer question was whether the regulation met the second part of the *Miller* test, which requires that, in order to be saved, the regulation must "substantially affect the risk pooling arrangement between the insurer and the insured." The court contrasted the copying cost regulation with those regulations that had been found saved because of their substantial impact on the benefits provided by the insurer, and reasoned the copying cost regulation did not meet the "substantially affect" requirement:

> There is one way that the California regulation could affect insurers' risks: By requiring insurers to pay copying costs, the regulation does make it slightly easier for insureds to file claims. If that causes more insureds to file claims, and if some of those

> additional claims are meritorious, then the regulation will cause insurers to pay more benefits than they otherwise would absent the regulation. But this possibility is too remote and speculative to "substantially" affect the risk pooling arrangement between insurers and their insureds. Few, if any, claimants will forgo a meritorious claim because of the relatively small expense of copying-so few, in fact, that they are unlikely to substantially affect the risk pool.

* * * *

Courts have struggled with determining whether an insurance regulation "substantially affects" the insured-insurer risk pooling arrangement. Some courts have treated the requirement almost as a tautology by reasoning that any limitation on the scope of permissible contractual relationships between the insured and insurer affects their risk pooling. The Ninth Circuit's requirement that the impact must be "substantial" in order for the regulation to be saved suggests the *Miller* risk pooling requirement may yet have some meaning.

Rulings, Filings and Settlements of Interest

- On July 2, 2008, UnitedHealth Group Inc. announced that it reached an agreement in principle to resolve the ERISA class action litigation relating to the company's alleged stock options backdating scheme for $17 million. The Company also announced an agreement in principle to pay investors $895 million to settle federal securities law claims against UnitedHealth for participating in the backdating scheme.

- In *Evans v. Akers*, No. 07-cv-1140, 2008 WL 2780607 (1st Cir. July 18, 2008), the First Circuit held that former employees who allege that fiduciary breaches reduced their lump-sum distribution from a defined contribution plan have standing to sue as "participants" under ERISA. In so holding, the court agreed with the Circuits that already had addressed the issue and rejected several arguments advanced by defendants.

- In *Chao v. Meixner*, No. 1:07-cv-0595-WSD (N.D. Ga. July 3, 2008), the district court granted the Department of Labor's request to certify for appeal the issue whether an ERISA Section 502(a)(2) claim is subject to a jury trial. The district court had earlier ruled it was, reasoning that relief seeking to impose personal liability to restore $150,000 in allegedly misappropriated plan assets was legal relief. In certifying this interlocutory decision for appeal, the district court concluded that there is a substantial ground for difference of opinion on whether jury trials are appropriate for claims brought under ERISA Section 502(a)(2).

- In *In re FremontGeneral Corp. Litig.*, 2008 WL 2609258 (C.D. Cal. May 30, 2008), the district court denied defendants' motion to dismiss plaintiffs' prudence and disclosure claims concerning the plan's retention of company stock. In so holding, the court reasoned that the Ninth Circuit, in *Wright v. Oregon Metallurgical Corp.*, 360 F.3d 1090 (9th Cir.2004), only set forth examples, not an exhaustive list, of what may make a company's stock an imprudent investment, and concluded that allegations the company faced dire financial circumstances and serious mismanagement were sufficient to state a claim in the instant case.
- In *In re Dell Inc. ERISA Litig.*, No. 06-cv-758, 2008 WL 2600175 (W.D. Tex. June 23, 2008), the district court granted Dell's motion to dismiss plaintiffs' prudence claims concerning the plan's retention of company stock, concluding that Dell did not breach a fiduciary duty to diversify because plan participants had complete discretion to invest participant and employer contributions to the plan. In so holding, the court reasoned that "to the extent the plan required diversification, it could only be at the level of investment options rather than asset distribution. Because the plan offers over a dozen investment options, it is diversified on its face." In addition, the court held that the participants were unable to overcome the presumption of prudence because the company's stock never suffered a "precipitous drop," and while Dell stock may not have been the best investment, there was no indication Dell's survival was ever threatened nor that Dell's stock was in danger of becoming worthless. The court refused, however, to dismiss the participants' disclosure claim notwithstanding defendants' contention that it was derivative of the prudence claims.
- In *Nauman v. Abbott Laboratories*, No. 04-cv-7199, 2008 U.S. Dist. LEXIS 54469 (N.D. Ill. July 10, 2008), the court held that former employees of Abbott Laboratories who were transferred to Hospira Inc. in 2004 with no rehire agreements can continue with their claim that Abbott undertook an "unlawful scheme" to transfer them to Hospira so as to deprive them of their right to pension and retiree health benefits. In so holding, the court acknowledged that each of the individual business steps taken by Abbott would not be enough alone to prove a violation of Section 510 of ERISA, which prohibits terminating a participant to interfere with his attainment of benefits. The court stated, however, that when those steps (including both the discharge and the no rehire agreement) were looked at as a whole, there was sufficient evidence presented that Abbott spun-off its hospital products division so as to reduce its benefits liability and deprive thousands of Abbott workers of pension and retiree health benefits.

Employee Benefits Litigation

Proskauer Rose's Employee Benefits Litigation Group is a significant component of the firm's renowned Labor and Employment Law Department, which has nearly 175 attorneys.

The Employee Benefits Litigation Group is led by Howard Shapiro and Myron Rumeld. The group defends complex and class action employee benefits litigation.

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