Proskauer

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We are pleased to announce that our New Orleans office will re-open on September 8, 2008. In the aftermath of Hurricane Gustav, all of our New Orleans personnel are accounted for and safe. Our e-systems remained on line during the Hurricane and remain on line now.

You may continue to communicate with all the lawyers in the New Orleans office via e-mail, BlackBerry, their work phone numbers, and their cell phones.

Editor's Overview

On the agenda for this month is an issue of perennial interest in ERISA litigation, cash balance claims, and an unusual case that extended to a welfare plan amendment ERISA's prohibition against cutting back accrued pension benefits.

In *Hurlic v. Southern California Gas Company*, the Ninth Circuit followed the four other circuits to rule (the Second, Third, Sixth, and Seventh) and concluded that the cash balance formula does not violate ERISA's prohibition against decreasing the rate of benefit accrual on account of age. The Ninth Circuit also held that the wear-away resulting from the cash balance conversion did not violate ERISA's anti-backloading requirement.

In *Battoni v. IBEW,* a New Jersey district court addressed whether an amendment to a welfare benefit plan which cut off retiree health benefits if a participant elected a lump-sum distribution from the pension plan violated ERISA's prohibition against cutting back accrued pension benefits under ERISA § 204(g). Although ERISA's statutory text explicitly excludes welfare plans from the coverage of ERISA § 204(g), the district court concluded that since this welfare plan amendment, in its view, was an indirect attempt to do what was otherwise prohibited by ERISA § 204(g), it should be treated as a "constructive or de facto" amendment to the pension plan prohibited by ERISA § 204(g).

Ninth Circuit Rules that Cash Balance Plans Are Not Inherently Age Discriminatory and that a Wear-Away Does Not Violate ERISA's Backloading Prohibitions

By Russell L. Hirschhorn

In the latest cash balance plan opinion, the Ninth Circuit, in *Hurlic v. Southern California Gas Company*, 2008 WL 3852685 (9th Cir. Aug. 20, 2008), concluded that Southern California Gas Company's ("SoCal") cash balance plan was neither age discriminatory nor impermissibly backloaded. The court did conclude, however, that plaintiffs stated a viable claim under ERISA's notice provision, section 204(h), and remanded the case for further proceedings.

The Ninth Circuit joined the Second, Third, Sixth and Seventh Circuits in concluding that cash balance plans do not violate the age discrimination provisions of ERISA. In light of the unanimous rulings of the five Circuits on this issue, it would appear that the Ninth Circuit's decision put the proverbial nail in the coffin on plaintiffs' age discrimination claim.

The Ninth Circuit also concluded that the SoCal cash balance plan, and in particular its wear-away provision, was not impermissibly backloaded in violation of the 133-1/3% rule — one of the three minimum accrual tests that a pension plan can satisfy which requires that benefit accruals do not increase by more than one-third in any particular year. In wear-away backloading claims, plaintiffs have contended that, by virtue of the cash balance conversion, the plan fails to satisfy the minimum accrual test requiring that benefit accruals do not increase by more then one-third in any particular year because there is a period of time – the wear-away period – in which there are no accruals, followed by a period in which ordinary accruals resume. The Ninth Circuit ruled that the backloading provisions were not implicated by the wear-away because of the special rule that states once there is an amendment to a plan, only the new plan formula is relevant when ascertaining if the plan satisfies the 133-1/3% rule. The Ninth Circuit's ruling mirrors one by the Third Circuit in the *PNC*litigation, but on different facts. The SoCal plan allowed employees' pre-conversion benefits to increase for five years before they were frozen by the wear-away, whereas the PNC plan did not allow for any pre-conversion accruals after the amendment to the cash balance. This distinction did not change the result according to the Ninth Circuit.

The Ninth Circuit did, however, remand the case to the district court for further consideration of the plaintiffs' section 204(h) claim, concluding that it was improperly dismissed since plaintiffs were entitled to notice of the wear-away provision and defendants admitted that no section 204(h) notice was given.

District Court Holds Amendment to Welfare Plan Violates ERISA § 204(g) when Amendment Was Adopted with Intent To Penalize the Exercise of Accrued Rights under the Pension Plan

By Robert Rachal

In *Battoni v. IBEW Local Union 102 Employee Pension Plan*, 2008 WL 3166697 (D.N.J. Aug. 8, 2008), the District Court addressed whether an amendment to a welfare benefit plan violated ERISA's anti-cutback provision of § 204(g), 29 U.S.C. § 1054(g), which prohibits plan amendments that purport to cut back accrued pension benefits. Because the court concluded that the welfare plan amendment was an indirect attempt to penalize the exercise of an accrued right to take lump sum benefits under the pension plan, the court concluded that this amendment fell under, and was prohibited by, ERISA § 204(g).

In *Battoni,* an underfunded pension plan offered by Local 675 merged with an overfunded pension plan offered by Local 102. The underfunded Local 675 plan permitted participants to take their pension benefits in a lump-sum, which right had to be carried forward after the merger because (at least for benefits accrued pre-merger) it was a protected accrued benefit under ERISA § 204(g)(2). The local unions also merged their welfare benefit plans. The welfare plan did not create any vested rights to retiree health benefits.

After several unsuccessful attempts to amend the merged pension plan to limit lump sum payments, the trustees amended the welfare plan to preclude payment of retiree welfare benefits for participants who elected a lump sum payment from the pension plan. The stipulated facts and testimony adduced at trial confirmed that the intent of this amendment was to accomplish indirectly what could not be done directly, *i.e.*, to impose a financial penalty for exercising the accrued right to take a lump-sum pension payment.

The district court concluded that, under these facts, the welfare plan amendment constituted a "constructive, indirect and/or de facto amendment" to the pension plan, prohibited by ERISA § 204(g). The court started by noting the anticutback rule is a "crucial" aspect of ERISA's protection of pension benefits, and that other courts had found ERISA § 204(g) violations even when there was no formal plan amendment. The court also cited an IRS regulation that prohibits the denial of protected accrued benefits through the "direct or indirect" exercise of discretion. Applying this "direct or indirect" rationale, the court concluded the trustees could not use an amendment to a welfare plan to indirectly effectuate a cutback to the accrued right to take a lump-sum benefit under the pension plan.

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Although *Battoni* appears to reflect the routine application of the legal principle that prohibits doing indirectly what cannot be done directly, it raises some problematic issues. First, *Battoni* failed to address that application of ERISA § 204(g) to an amendment to a welfare plan is contrary to the plain language of ERISA. ERISA § 204(g) is part of Part 2 (Participation and Vesting) of Title I of ERISA. ERISA § 201(1), 29 U.S.C. § 1051(1), explicitly excludes "welfare plans" from the coverage of Part 2. Second, plan sponsors often consider their benefit packages holistically, and factor in that cost reductions which may be unlawful under a pension plan may be permitted under a welfare plan. Once the limitations embodied in the statutory text are bypassed through the application of "indirect" theories of liability, there is potential room for substantial mischief, as amendments that comply with ERISA's complex statutory rules may be able to be scrutinized for intent and claimed indirect effects.

Rulings, Filings and Settlements of Interest

- In *Lanfear v. Home Depot Inc.*, 2008 WL 2916390 (11th Cir. July 31, 2008), the Eleventh Circuit joined several other Circuit Courts to conclude former participants have standing to pursue fiduciary breach claims seeking losses from alleged imprudent plan investments in employer stock. The court also reaffirmed its view that claims for breach of fiduciary duty must be exhausted through the plan's administrative review process before suit may be filed.

- In *Vaughn v. Air Line Pilots Association, International*, 2008 U.S. Dist. LEXIS 56741 (E.D.N.Y. July 24, 2008), the district court held that ALPA did not violate Sections 4(c) and 4(i) of the ADEA, 29 U.S.C. §§ 623(c), 623(i), with respect to the pension benefits offered the airline pilots. In so holding, the district court rejected plaintiffs' claim that the defined contribution plan was age discriminatory since younger pilots will receive more retirement benefits than older pilots. The court reasoned that plaintiffs' harm was premised solely on the fact that older pilots will work fewer years than younger pilots, and thus will ultimately accrue less retirement benefits.
- In *Stanford v. Foamex L.P. et al.,* No. 07-4225, 2008 WL 3874823 (E.D. Pa. Aug. 20, 2008), the district court declined to dismiss claims that defendants, the plan fiduciaries and the directed trustee, breached claimed fiduciary duties when they *sold* employer stock of a company that had filed for bankruptcy. Plaintiff claimed that the sales were contrary to the plan terms requiring the employer stock fund be invested primarily in employer stock. The district court concluded it was unprepared to rule on a motion to dismiss that *Moench* permitted these sales as a matter of law. The court, however, dismissed the claim that the plan fiduciaries allegedly misled participants about the divestment of the employer stock fund, concluding that plaintiff's allegation he was prevented from being able to make fully informed investment decisions failed to allege reliance with sufficient particularity.
- In *McCoy v. Health Net Inc.*, 2008 U.S. Dist. LEXIS 60446(D.N.J. Aug. 8, 2008), the district court approved one of the largest ERISA settlements on record. As part of the settlement, Health Net is required to establish a $215 million cash fund and to change its business practices in determining "usual, customary, and reasonable" data used to calculate copayments for out-of-network health services.

In *Redington v. Goodyear Tire & Rubber Co.*, No. 07-1999, 2008 U.S. Dist. LEXIS 64639 (N.D. Ohio Aug. 22, 2008), the district court approved the settlement of a declaratory action for retiree health benefits for over 30,000 union-represented Goodyear retirees. The action arose out of labor negotiations and resolution of a strike in which Goodyear agreed to fund a VEBA with a
$1 billion payment by Goodyear. The court concluded the settlement was fair, reasonable and adequate in light of the litigation risk that retirees may be unable to prove their retiree medical benefits are vested benefits, while the VEBA funding avoided the business risks that Goodyear could become unable to fund these benefits in the future

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