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Managing ERISA Risk: Best Practices Learned from Courts

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Opening Observations



- Many judges misunderstand or dislike ERISA cases, and their decisions on unsettled issues can be erratic or contradictory
- The Supreme Court is more and more interested, addressing a broad range of ERISA-related topics
- It is essential to take notice of what the Court has settled:
 - Litigation can be averted
 - Quick dismissals may be available
 - Excessive damage awards may be avoided

Topics to be Covered

1. Litigation Risk Management in Plan Design
2. The New Rules of Fiduciary Prudence
3. Our Disclosures about Your Disclosures
4. Our Claims about Processing Your Claims
5. Changing Benefits to Keep up with Changing Times

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Today's Topics

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Plan Design: Overview



- Judicial decisions offer insights into the implications of common—and unusual—plan terms.
- Just as new techniques for mergers are incorporated into M&A transactions, new techniques for avoiding ERISA risks should be incorporated into plan documents
- Courts uniformly view an ERISA plan document as a binding contract, except to the extent that the plan would violate ERISA

Plan Design: Issues that Matter

- Establishing contractual time limits on claims
- Determining a preferred judicial venue
- Selecting who is a fiduciary—and who is not
- Recouping benefit overpayments
- Prohibiting benefit assignments

Plan Design: ERISA's Limitations Periods

Fiduciary breach claims:

**3 years
after discovery**

**6 years
after breach**

whichever is earlier

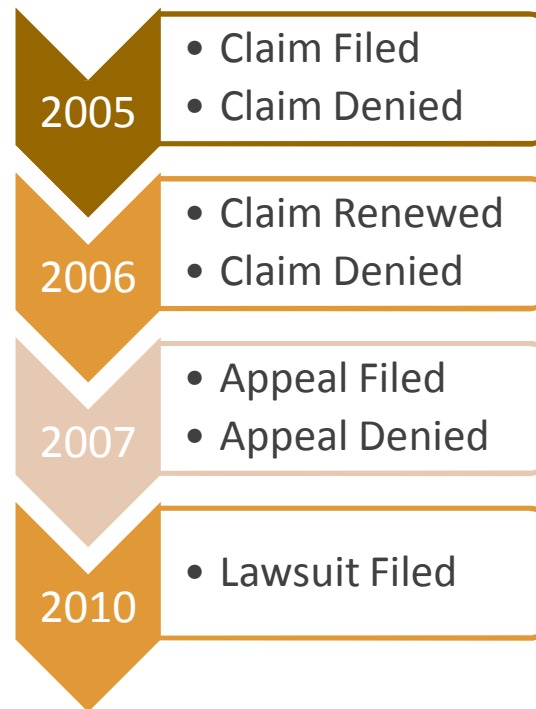
Benefit claims:

**Apply
State Law**

Plan Design: Contractual Limitations Periods

Heimeshoff v. Hartford Life

“Legal action cannot be taken ... [more than] 3 years after the time written proof of loss is required to be furnished.”



Plan Design: Contractual Limitations Periods



- Limitations clause upheld
- Nothing in ERISA displaces state law on contractual limitations provisions
- Contract law favors negotiated limitations periods, so long as they are reasonable
- The public policy underlying ERISA likewise supports allowing employers freedom to design their own plans

Plan Design: Lessons from *Heimeshoff*



- The Take-Aways
 - Consult state law
 - Consider a contractual limitations period for the plan document
 - Complete administrative review promptly
- From the Lower Courts
 - A deadline of one year after administrative review is reasonable; shorter periods may be unreasonable
 - For administrative delays, equitable tolling may be appropriate, and is a question of fact
 - Reasonableness of contractual limitations period may be a question of state law

Plan Design: Venue

- ERISA § 502(e)(2) authorizes plaintiffs to choose venue:
 - Where the plan is administered
 - Where the alleged violation occurred
 - Majority View: Where plaintiff received or would receive his benefits. *E.g., Cole v. Cent. States Se. & Sw. Areas Health & Welfare Fund*, 225 F. Supp. 2d 96, 98 (D. Mass. 2002)
 - Minority View: Where payment decisions are made. *Turner v. CF&I Steel Corp.*, 510 F. Supp. 537, 541 (E.D. Pa. 1981)
 - Anywhere the defendant can be found
- Plaintiffs use this broad provision strategically

Plan Design: Picking Your Venue



- Can venue be changed by the plan document?
 - *Smith v. Aegon Cos. Pension Plan* (6th Cir. 2014): Yes, so long as it's fair
 - Consumer Financial Protection Board: It is “abusive” to include venue-selection clauses in adhesion contracts; CFPB has sought authority over retirement accounts
- Practical considerations
 - Check the law before picking a particular forum, including the state limitations period for benefit claims
 - Check the law in the particular forum where the case was filed
 - Consult the “choice of laws” rules in your preferred venue

Plan Design: Picking Your Defendants



- Threshold Question: When plaintiffs file suit for breach of fiduciary duty, they can sue only plan fiduciaries
- Those fiduciaries will be subject to depositions and other discovery obligations and burdens
- Who is on the hook?
 - Named fiduciaries identified in the plan documents
 - Those who exercise discretion over plan assets/administration
 - Those who appoint fiduciaries
- Consider protecting officers who appoint ERISA fiduciaries through careful plan structure
- Will the rules change with new DOL guidance?

Plan Design: Picking Your Defendants



- *Johnson v. Couturier* (9th Cir. 2009)

[W]here members of an employer's board of directors have responsibility for the appointment and removal of ERISA trustees, those directors are themselves subject to ERISA fiduciary duties, albeit only with respect to trustee selection and retention

- *Newton v. Van Otterloo* (N.D. Ind.): directors' duty arises only upon

“notice of possible misadventure by their appointees”

- Guidance from *Tibble* on scope of the duty to monitor?

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Fiduciary Prudence: Key Areas of Litigation



- Vendor Selection and Monitoring
- Investment Selections
- Company Stock

Fiduciary Prudence: General Rules



- Courts aren't well situated to evaluate outcomes
- Instead of assessing substantive prudence, courts will often evaluate procedures employed
 - Won't second-guess a decision if it followed a prudent process (e.g., *George v. Kraft* (7th Cir.) (unitized company stock))
 - Will find liability if a prudent process was *not* followed (e.g., *Tibble v. Edison* (9th Cir.) (mutual-fund fee negotiation))
- A finding that fiduciaries were insufficiently attentive will often cause courts to conclude that outcome was poor
 - E.g., *Tussey v. ABB* (8th Cir.) (implicit recordkeeping fees)

Fiduciary Prudence: Considerations

- Evidence of prudent process even more critical
 - Who is on plan committee?
 - Advisors (*but cf. George v. Kraft*)
 - Independent review of advisor's analysis
 - In-depth deliberations
 - Detailed records
 - Caution: Fiduciary exception to attorney-client privilege
 - Test is not who pays for legal advice
 - Advice given for fiduciaries' own protection is easier to defend
 - Consider retaining separate counsel for Committee and Plan Sponsor on ERISA issues
- Should you retain an independent fiduciary? For what scope?

Fiduciary Prudence: Company Stock



- The Way It Used To Be (*Moench*)
 - Because company stock gets favorable treatment under ERISA, decision to offer company stock is presumptively prudent
 - Only dire circumstances could support stock-drop liability
- The Way it Is Now (*Dudenhoeffer*)
 - There is no presumption of prudence
 - To sue a public company , a plaintiff must show special circumstances that made it imprudent to follow the market
 - Fiduciaries aren't required to violate securities laws
- Also: Litigation on Structuring of Company Stock Funds

Fiduciary Prudence: Interpreting *Dudenhoeffer*



- *Harris v. Amgen* (9th Cir., post-*Dudenhoeffer*)
 - Plaintiffs can state a claim based on imprudence of investment in employer stock
 - Plaintiffs can state a claim for breach of fiduciary duty by alleging a violation of Section 10(b) of the Securities Exchange Act of 1934
 - When Form S-8 prospectus is incorporated by reference into the Summary Plan Description, misstatements in Forms 8-K and 10-K are fiduciary misstatements redressable under ERISA
 - *Petition for Rehearing En Banc is pending*
- Similar district court decisions in NY and Illinois

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Participant Disclosures: Basics



- Fiduciaries must act solely in the interests of participants
- The written plan instrument governs fiduciaries
- Fiduciaries must alert plan participants as to the key components of their plan (*e.g.*, through Summary Plan Descriptions)
- Potential liability if the disclosures misstate the plan’s terms
 - Law focuses mostly on intentional misrepresentations
 - Posner, J.: “[S]lipups in managing any complex enterprise are inevitable, and negligence—a violation of the duty of care—is not actionable.

Participant Disclosures: *CIGNA Corp. v. Amara*



- Pre-*CIGNA*: Plan participants can file suits for “benefits” based on the terms of their SPDs
- *CIGNA*
 - The formal plan document defines “benefits” (§ 502(a)(1)(B))
 - But it’s still a fiduciary breach to misinform plan participants
 - Relief for these breaches is limited by the rules of equity
 - Previously, *Russell, Mertens, Great-West*: No recovery of money damages
 - Today, *CIGNA*: Although money damages are “legal,” not “equitable,” there are equitable remedies that have the effect of transferring money

Participant Disclosures: Remedies post-*CIGNA*



- Reformation (*e.g., Amara v. CIGNA* (on remand))
 - Plan can be equitably “reformed” to comply with faulty disclosures; requires a showing of fraud or mutual mistake
- Surcharge (*e.g., Skinner v. Northrop*)
 - Payment of money by fiduciary for misconduct; requires a showing of fiduciary duty, reliance, and injury
- Estoppel (*e.g., Gabriel v. Alaska Elec. Pension Fund*)
 - Requires a showing of reliance
- Constructive Trust (*e.g., Liss v. Fidelity Empl. Servs. Co.*)
 - Recovery of identifiable property that belongs to another; requires identifiable property; at court’s discretion

Participant Disclosures: Making the SPD binding



- Per *CIGNA*, the SPD is not the “plan” and cannot be enforced as the plan
 - *Caveat*: Courts may enforce the SPD if there is no written plan
- But that cuts both ways—there may be circumstances in which the employer *prefers* for the SPD to govern
 - There is no lengthier document
 - There are concerns about inconsistencies between the two documents
- In some circumstances, the SPD should be incorporated by reference into the formal plan document

Participant Disclosures: Regulatory Changes



- 408b-2 Fee Disclosures for Plan Sponsors
 - Plan sponsors must obtain disclosures from vendors of all fees directly and indirectly charged to plan participants, and make appropriate determinations based on these disclosures
 - Indirect fees may include:
 - Revenue sharing (legal, but question of conflict of interest)
 - Float
 - Proceeds of securities lending
 - Use RFP process for vendor selection; reevaluate periodically
- 404a-5 Fee Disclosures for Plan Participants
 - Annual disclosure of investment performance, benchmark, and fee data

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Claims: Addressing overpayments

- Mistakes in benefit calculations inevitably happen
- You want to be able to recoup overpayments
 - Health plans: Overpayments to providers
 - Retirement plans: Miscalculations of benefits
- Default rule under ERISA: Equitable lien/constructive trust is available only if the funds can be traced
- **WHAT YOU CAN DO:**
 - An equitable lien can be established by agreement
 - Address this issue in the plan by requiring recoupment

Claims: Addressing overpayments



- **WHAT YOU CAN DO:**

- Consider invoking the IRS's Voluntary Correction Program
- Make the plan whole from company assets
- Document a careful cost/benefit evaluation in deciding whether to recoup

Claims: Remember ERISA's special privilege rules



- Under ERISA, when legal advice is given for purposes of plan administration, the attorney-client privilege belongs to plan participants
- Unless legal advice is for fiduciary's own interest, it likely will be for the benefit of the plan participants
- Legal advice in connection with internal claims procedure is typically not privileged

Claims: Giving yourself deference



- Standards of review matter
- Default rule: *De novo* review of interpretations of plan terms
- *Firestone Tire v. Bruch*: Plan document can authorize fiduciaries to exercise discretion in interpreting plan terms, in which case abuse of discretion review applies
- Some courts have extended *Firestone* to plan interpretations in fiduciary-breach cases
- **BOTTOM LINE:** Give yourself deference to interpret the plan

Claims: Giving yourself deference



The Committee shall have the responsibility, and the full power and authority, to determine in its sole discretion, all questions concerning the construction and interpretation of the Plan and its administration, including, but not by way of limitation, the determination of the rights or eligibility of claimants and beneficiaries, and the amount of their respective benefits, and to make factual findings.

Claims: Avoiding conflicts of interest

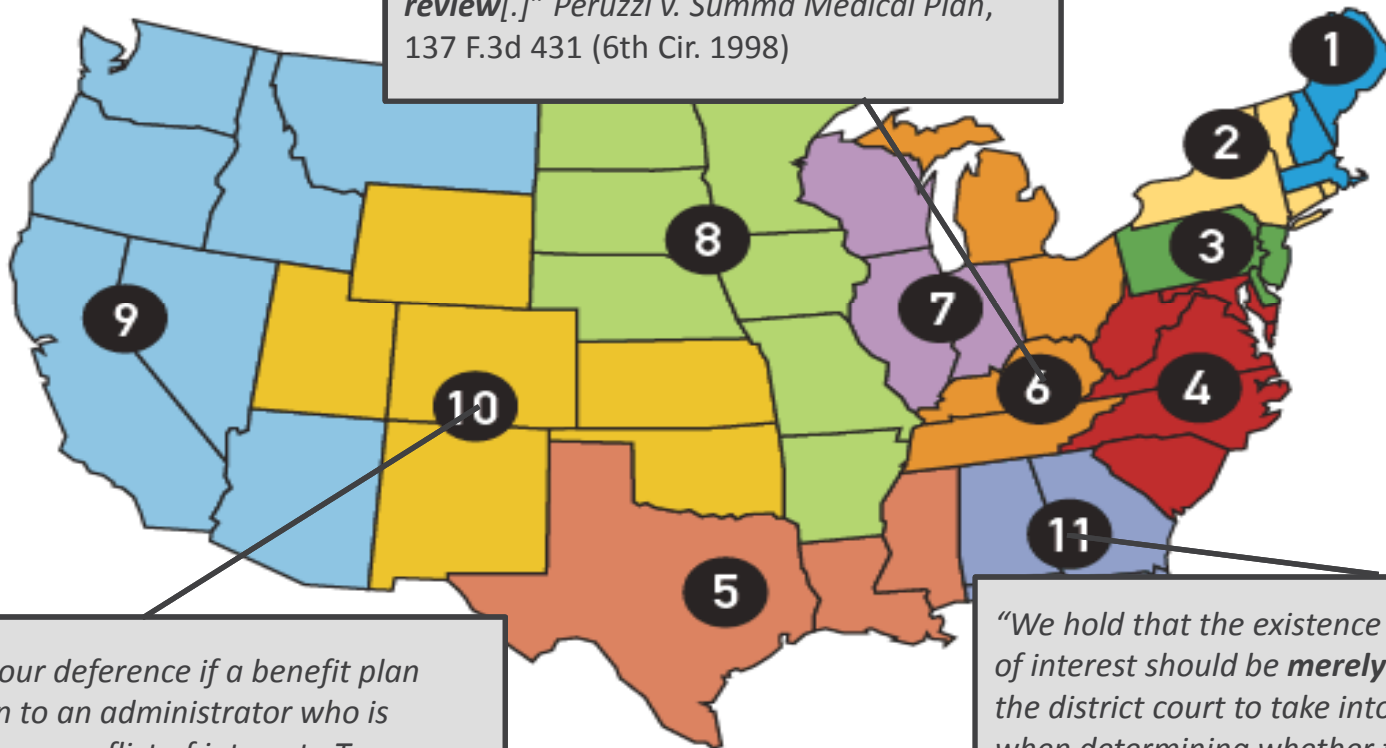


- *MetLife v. Glenn*: When the fiduciary assessing claims has a financial stake in the decision, there is a conflict of interest
- *Firestone* deference still applies, but:
 - Courts can take into account the conflict in assessing whether there has been an abuse of discretion
 - Discovery may be warranted to assess conflicts

Claims: How *Glenn* Is Applied

Abuse of Discretion When Conflict Exists

"The conflict of interest inherent in self funded plans does not alter the standard of review[.]" Peruzzi v. Summa Medical Plan, 137 F.3d 431 (6th Cir. 1998)



*"We dial back our deference if a benefit plan gives discretion to an administrator who is operating under a conflict of interest. To incorporate this factor we have crafted a **sliding scale approach**. Weber v. GE Group Life Assur., 541 F.3d 1002 (10th Cir. 2008)*

*"We hold that the existence of a conflict of interest should be **merely a factor** for the district court to take into account when determining whether the administrator's decision was arbitrary and capricious." Doyle v. Liberty Life Assur., 542 F.3d 1352 (11th Cir. 2008)*

Claims: Avoiding conflicts of interest



- Consider Third-Party Claims Administrators
- Review the Composition of Benefits Committees
 - Avoid high-level corporate executives with involvement in corporate finance
 - HR personnel responsible for ethics or compliance may be particularly well-suited
- Review Claims Procedures
 - Bifurcate initial claims decision from appeal
 - Consider shielding dollar value of claim from appeal panel

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Changing Benefits: Retirees



- In changing economic conditions, companies often look for ways to reduce benefits costs
- A common consideration is whether to reduce retiree medical benefits, by:
 - Terminating or limiting coverage
 - Increasing retiree contributions
- Critical question is whether lifetime benefits were promised
 - In the plan document
 - In plan disclosures

Changing Benefits: Retirees

- The Sixth Circuit previously applied the *Yard-Man* presumption: Retiree health benefits are vested, cannot be altered after retirement
- Supreme Court rejected *Yard-Man* in *M&G Polymers v. Tackett* (2015): Ordinary contract rules determine whether retiree benefits have vested
 - Justice Thomas: Retiree health benefits are not deferred comp and are not tied to the duration of the pension benefits; public policy requires enforcement of parties' intentions
 - Justice Ginsburg: Even without an inference, there are provisions that contemplate vested coverage

Changing Benefits: ERISA § 204



§ 204(g) The accrued benefit of a participant under a plan may not be decreased by an amendment of the plan

- Prohibits any amendments that make the accrued benefit “less valuable,” regardless of whether there is an actual decrease in payments.
- Narrowing the range of permitted post-retirement employment is a decrease in benefits. *Cent. Laborers' Pension Fund v. Heinz* (2004).

Changing Benefits: ERISA § 204



§ 204(h) An applicable pension plan may not be amended so as to provide for a significant reduction in the rate of future benefit accrual unless the plan administrator provides [adequate] notice.

- In light of the detailed implementing regulations promulgated in 2003 (26 C.F.R. § 54.4980F-1), courts will be reluctant to read extra requirements into the statute. *Tomlinson v. El Paso Corp.* (10th Cir. 2011).

Changing Benefits: Pension De-Risking



- Managing a defined-benefit plan can be costly and risky, particularly during periods of low interest and high volatility
- Plan sponsors may want to liquidate risks
 - Buy out annuitants
 - Outsource payments with a group annuity contract
- First challenge: *Verizon*
 - Change in payor is not a loss of benefits
 - Claims that annuity was too expensive greeted with skepticism
 - Participants remaining in the plan lack standing

Changing Benefits: Pension De-Risking



- A plaintiff challenging pension de-risking must identify how he has been harmed, which may be difficult
- But plan sponsors must be careful to follow a prudent process in evaluating and implementing a de-risking plan
- Consider the use of an independent fiduciary

Questions?

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