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BNA, Inc.

Pension & Benefits

DAILY

Volume 08 Number 116
Tuesday, June 17, 2008
ISSN 1523-5718

Legal News

Cash Balance Plans

Court Addresses Relief for Deficient Notice Of Conversion; Stays Order Pending Appeal

The U.S. District Court for the District of Connecticut issued June 13 its ruling as to the remedies that are available to participants in a cash balance plan sponsored by CIGNA Corp. who were not provided with timely and accurate information about the plan's conversion from a traditional defined benefit plan to a cash balance plan (*Amara v. CIGNA Corp.,* D. Conn., No. 3:01CV2361 (MRK), 6/13/08).

Judge Mark R. Kravitz rejected the participants' contention that the proper remedy was to return the plan to a traditional defined benefit plan formula, as if the amendment converting the traditional defined benefit plan to a cash balance plan had never happened. Kravitz found, however, that the participants should have their benefits recalculated using both the traditional defined benefit formula and cash balance formula, but he ordered that the remedies detailed in his opinion be stayed pending appeal to the U.S. Court of Appeals for the Second Circuit.

CIGNA converted its traditional defined benefit pension plan to a cash balance plan in 1998. Prior to the conversion, participants in the traditional defined benefit plan who met certain age and service requirements could receive a subsidized early retirement benefit.

When it converted to a cash balance plan, CIGNA "froze" the benefit accruals of employees with a combined age and years of service less than 45. Employees who had age and service credits of 45 or more were "grandfathered" under the traditional defined benefit plan and continued to accrue benefits under the plan.

Nongrandfathered employees were transferred to the new cash balance plan, the court said. When they severed their employment with CIGNA, the nongrandfathered participants were entitled to receive the "greater of" their benefits under the traditional defined benefit plan or the cash balance plan. Unlike the traditional defined benefit plan, the cash balance plan offered participants the option to receive their benefits in a lump-sum distribution. To receive a lump-sum distribution, however, the participants would not be eligible for the subsidized early retirement benefits.

Plan Doesn't Discriminate but Notice Deficient

A group of participants filed a lawsuit in 2001 contending that the cash balance plan was age discriminatory, violated the Employee Retirement Income Security Act's anti-backloading rule, and resulted in the forfeiture of accrued benefits. The participants further alleged that CIGNA's notice of the plan conversion did not comply with ERISA.

In December 2002, the district court certified the lawsuit as a class action consisting of approximately 25,000 CIGNA employees and retirees (6 PBD, 1/10/03 ; 30 BPR 87, 1/14/03; 29 EBC 2208).

Just over six years later, the district court in February 2008 addressed the merits of the participants' lawsuit and found that the cash balance plan did not discriminate against older workers or violate ERISA's anti-backloading rule. The court found in that decision, however, that CIGNA violated ERISA's notice and disclosure requirements when it gave the participants notice of the plan conversion without explaining, for example, that the plan would result in a "wear away" of benefits for some participants (33 PBD, 2/20/08 ; 35 BPR 469, 2/26/08; 43 EBC 1011).

In particular, the court in that decision found that the notices CIGNA provided about the plan conversion did not comply with ERISA Section 204(h), which prohibits plan amendments that provide for a significant reduction in the rate of future benefit accruals unless the plan administrator gives at least 15 days notice prior to the effective date of the amendment.

In addition, the court found in that decision that CIGNA violated ERISA Section 102's requirements for summary plan descriptions and summaries of material modifications. CIGNA had a duty to inform participants of the possibility of wear away in its SPDs and SMMS, the court said. The court found that CIGNA was required, but failed, to inform participants that lump-sum distributions under the cash balance plan did not include any early retirement benefits. CIGNA was not required, however, to inform participants of whether the annuity option for distribution was more valuable than the lump-sum option, the court said. In this earlier decision, the court held off in determining what remedies were available to the participants for CIGNA's violation of ERISA's notice and disclosure requirements.

What Is the Remedy for Noncompliant Disclosure?

In its most recent decision, the court discussed in detail the remedies available to the participants for CIGNA's violation of the notice and disclosure requirements of ERISA. The court refused, however, to grant the participants' request that the cash balance plan be rescinded in its entirety to remedy CIGNA's failure to comply with Section 204(h).

According to the court, the amendments at issue were "unusual, if not unique" because CIGNA implemented the cash balance plan by first using an amendment to "freeze" benefit accruals under the traditional defined benefit plan, then issued a second amendment adopting the cash balance plan. The court said the freeze "served essentially as a placeholder" and was intended to disappear once the cash balance plan became operative. "The Court is aware of no other case, at least in this circuit or perhaps nationally, in which such a freeze was implemented in the process of transitioning to a cash balance plan," the court noted.

The court said it was "particularly reluctant" to order a "widespread return" of plan participants to the traditional plan as a remedy for the Section 204(h) violation given that the cash balance plan itself was legally valid under ERISA and CIGNA had provided substantially accurate information to its employees through the amendment it used to freeze benefits before it officially converted to a cash balance plan.

"[T]he Court is faced here with a situation in which the apparently exclusive remedy of invalidation [of the cash balance plan] would harm, rather than benefit, Plaintiffs, for the result would be a return not to a viable benefit plan, but to a freeze," the court said.

The court added that it "wished to emphasize" its concerns about CIGNA's use of a freeze. "[B]y upholding the validity of the freeze amendment, and consequently not ordering the invalidation of [the cash balance plan], the Court has permitted CIGNA effectively to eviscerate the notice requirements of §204(h)," the court said.

Court Orders Issuance of New Notices

Moreover, the court said that while it had determined that a return to the traditional defined benefit plan was not an appropriate remedy for CIGNA's violation of Section 204(h), CIGNA must issue new Section 204(h) notices to plan participants. "The Court understands that a §204(h) notice is usually due at the time of the amendment or not at all. However, especially in light of the Court's determination that invalidation of [the cash balance plan] is not warranted, the Court believes that plan participants at least deserve to know, albeit belatedly, the true effect on their retirement benefits of the transition" to the cash balance plan, the court said.

The court went on to say that the proper remedy for CIGNA's failure to issue SPDs and SMMS that complied with ERISA was to grant the participants benefits using an "A+B" formula under which they would receive all of their traditional defined benefit plan benefits in the form those benefits were previously offered prior to the conversion, plus all the benefits that accrued under the cash balance plan. In so ruling, the court rejected CIGNA's suggestion that the court order the recalculation of opening account balances using the same formula as that applied to participants with 55 or more age and service points. This approach "would not remedy CIGNA's misrepresentations regarding the inclusion of all early retirement benefits--that is, in the opening account balances, the age 62 benefit, rather than the age 55 benefit, would be used," the court said.

In addition, the court ordered CIGNA to issue updated and corrected SPDs, and to provide new, accurate benefit election notices to participants that reflected the court's determinations regarding the appropriate procedure for providing additional benefits. The court added that any class member who has already retired and commenced receiving benefits would be entitled to prejudgment interest on any benefits due between Jan. 1, 1998, and the date of judgment.

The court concluded, however, that the remedies set out in its decision will be stayed pending review of the court's decision by the Second Circuit. "The remedy issues addressed in this decision are complex, difficult, and enormously important to employers and employees alike," the court said in staying its judgment so that the parties could proceed to the Second Circuit for further guidance. "The stakes are far too high--for both CIGNA and its employees--to implement the Court's judgment in the face of such substantial uncertainty," the court added.

The participants were represented by Stephen R. Bruce and Allison C. Caalim of Law Offices of Stephen R. Bruce, Washington, D.C., and Thomas G. Moukawsher of Moukawsher & Walsh, Hartford, Conn.

CIGNA was represented by Bradford S. Babbitt and Brett J. Boskiewicz of Robinson & Cole, Hartford, Conn.; Jeremy P. Blumenfeld, Joseph J. Costello, and Jamie M. Kohen of Morgan, Lewis & Bockius, Philadelphia; and Christopher A. Parlo of Morgan, Lewis & Bockius, New York.

The full text of the opinion is at http://pub.bna.com/pbd/301cv2361c.pdf.

By Jo-el J. Meyer

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ISSN 1523-5718