Explaining Plan Changes: Lessons from the Supreme Court in *CIGNA v. Amara*

Anne E. Moran

Whether via electronic or paper media, or in televised town hall meetings or focus groups, participant communication is always a challenge for employers and plan sponsors. Although most legal scholars are focusing on the impact that the recent Supreme Court case of *CIGNA Corp. v. Amara, et al.*[1] may have with respect to remedies available to participants due to faulty plan communications, the facts of the case also illustrate the need for plan administrators and service providers to be extremely careful when describing changes in plan documents to participants.

Background

At first glance, the case of *CIGNA Corp v. Amara* could be seen as one of those textbook procedural cases that justify the characterization of benefits lawyers as technocrats who engage in heated conversations using terms such as "502(a)(1)(B) relief" versus "502(a)(3) relief" and "appropriate equitable remedies available in the days of the divided bench." But in the context of these technical discussions, the Supreme Court struggled with a number of basic issues—whether a summary plan description (SPD) is part of the plan document, and what relief should be available under the Employee Retirement Income Security Act (ERISA) when plan communications are "downright misleading." A review of the facts of the case also provides a primer on the proper and improper methods of participant communications.

The case involved the 1998 conversion of a traditional defined benefit pension plan sponsored by CIGNA Corporation (CIGNA) into an account-based cash balance plan. The traditional plan's benefits were based on a formula that took into account compensation, age, and service. Individuals who met certain criteria stipulated in the plan were eligible at age 55 for a "subsidized" early retirement benefit; *i.e.*, the benefit payable at normal retirement age would be reduced significantly less for early payment than would otherwise be actuarially appropriate.

Anne E. Moran is a partner at Steptoe & Johnson LLP in Washington, DC. She advises clients on executive compensation issues and on benefits issues arising under retirement, health, and other benefit plans. Over the course of her career, she has served as Tax Counsel for the Senate Finance Committee and on the ERISA Advisory Council for the Department of Labor. Ms. Moran may be reached at *amoran@steptoe.com*.

The cash balance formula that replaced this traditional formula as of January 1998 contained an opening account balance which the plan communications described as being equivalent to the amount accrued under the traditional defined benefit plan as of December 31, 1997. After 1997, annual contributions were to be made to the accounts of each participant based on the participant's age and service. The plan had a provision stating that participants would never receive less under the cash balance plan than the accrued benefit under the defined benefit plan on the date of change. This provision was designed to comply with the anti-cutback rule of Internal Revenue Code (Code) Section 411(d)(6).

CIGNA sent a newsletter explaining portions of the intended changes to participants in 1997. Additional information about the new formula was provided in a SPD in 1998. No one challenged CIGNA's authority to amend the plan. Rather, a class action lawsuit was filed on behalf of 25,000 participants challenging the new plan based on alleged false and misleading communications about the plan and the effect of its changes.

The district court issued more than one decision in this case. In its so-called Liability Decision of over 50 pages, the court found that the SPD and other disclosure materials were "inadequate under ERISA and in some instances, downright misleading."[2] A variety of statements were made in connection with the introduction of the new plan, including statements that the new plan builds benefits "faster" than the old plan, that CIGNA would not recoup cost savings from the changes, that the new plan works well for both shorter service employees and longer-service employees, and that there would be "growth in your total retirement benefits from CIGNA every year."

CIGNA admitted that it did not inform employees that certain participants might not accrue benefits under the new plan for a number of years due to the grandfather of the old plan's accrued benefit. It is not unusual for a cash balance plan's "grandfathered" accrued benefit as of the date of change to exceed the new account-based benefit for a few years. When a pension plan formula is amended, under ERISA and the Code, the benefit must be the greater of the benefit under the new formula or the frozen grandfathered benefit (as of the date of change) with any actuarial increases based solely due to the passage of time. In CIGNA's plan design, the initial account balance did not reflect the full value of certain features of the plan such as the early retirement benefit. Although this design may be permitted in a cash balance plan, it makes it more likely that the grandfathered benefit would remain higher for a number of years. Employees were also not specifically told that the traditional plan's early retirement subsidy would not be reflected in the new cash balance plan account.

In addition, despite the statements to employees that CIGNA would not enjoy cost savings from the change, it was estimated that the company apparently would save approximately $10 million of future plan

expenses due to the conversion to a cash balance plan, although CIGNA maintained that a comparable amount would be used elsewhere to enhance its other retirement plans.

In addition, a number of these inconsistencies and omissions in plan communications may not have been unintentional and might have been reduced. Certain managers who had met with employees and participant focus groups had indicated that there was confusion about the effect of the plan change, and requests were made for illustrations that would demonstrate the impact of the change, but this was not done. Employee responses to a questionnaire about the 1997 communications kit also indicated a desire to see illustrations, comparisons, and projections of the old and new formulas. Some of this requested information would have to be provided under current Internal Revenue Service (IRS) regulations; it should be noted that at the time of the 1997 disclosures, the regulations under ERISA Section 204(h) that describe how plan changes must be communicated were not as explicit as they are today.[3]

District Court Decisions

The district court's Liability Decision held that the disclosures were not written in a manner that satisfied ERISA. Specifically, the court held that the notices failed to satisfy the ERISA Section 204(h), requiring administrators to provide participants with a notice of a significant reduction in the rate of future benefit accruals that contained the text of the amendment or that summarized its effects. Moreover, the court held that the plan fiduciaries failed to provide an SPD and summary of material modifications written in a manner calculated to be understood by plan participants and that "reasonably apprise such participants and beneficiaries of their rights and obligations under the plan."

CIGNA maintained that even if the disclosures were ineffective, the plaintiffs were not entitled to relief because they did not demonstrate reliance on the SPD or any injury.

The district court disagreed with CIGNA, stating that under ERISA the standard was whether the plaintiff's demonstrated "likely harm." This standard was met, the court maintained, because the information provided likely led participants to believe that their combined benefits from the two plan formulas would be comparable to the old plan and that they would earn benefits each year. The court did not require a showing of financial harm.

Based on these facts, the court issued its decision on remedies, which it characterized as "complex, difficult, and enormously important to employers and employees alike."[4] The district court's remedy was to "reform" the plan to conform the document to the descriptions provided to participants, and to order the plan administrator to pay benefits in accordance with the reformed plan. This relief was based on ERISA Section 502(a)(1)(B), which gives a plan participant the right to "recover benefits due to him

under the terms of his plan ... or to clarify his rights to future benefits under the terms of the plan." Because of this determination, the district court declined to discuss whether a remedy was available under ERISA Section 502(a)(3), which provides for "other appropriate equitable relief." The court noted that prior court precedents significantly limited the scope of equitable relief, and that such relief may not be able to include money damages. The parties did not argue for, and the district court did not use, the legal remedy for Section 204(h) violations—rescission of the amendment—in this case. This is because it appears that the actual amendment freezing the old plan's benefits was adequately explained, so it was believed that the "section 204(h) remedy" would have resulted in freezing of the old plan without any new plan benefits.[5] On appeal, the Second Circuit affirmed the district court's decision.

Supreme Court Analysis

A unanimous Supreme Court (with Justice Sotomayor recusing) vacated and remanded the district court's decision on appropriate remedies. The Court held that errors in an SPD cannot be enforced under ERISA Section 502(a)(1)(B) of as a contractual claim for benefits. This is because the SPD is not considered part of the plan document, so cannot be part of the "contract" with participants. The Court distinguished the roles of the SPD and the plan, stating that the plan document was designed to set forth contractual terms and conditions of participation and that by contrast, the SPD was intended to summarize the terms of the plan and provide a communication to employees. The Court stated that enforcement of the terms of the SPD as a plan document could lead plan administrators to "sacrifice simplicity and comprehensibility in order to describe plan terms in the language of lawyers," and might defeat the purpose of the SPD—that is, to summarize and describe the plan.

Because the Court disallowed the district court's remedy of enforcing a required contract based on the SPD, the case had to be remanded so that the district court could consider what remedies were appropriate. However, a majority of the Supreme Court also went on to review the possibility that an equitable remedy under ERISA Section 502(a)(3) might be available, and to interpret the scope of that section, "given the likelihood that on remand, the district court will turn to and rely upon this alternative."

By way of background, it should be noted that "equitable relief" has been interpreted by the American courts to include the type of relief that was usually provided by British courts of equity. In contrast to "law courts," which were designed to enforce the laws of the land, the courts of equity (sometimes called chancery courts) were originally separate courts that handled petitions that required remedies (such as injunctions and specific performance) other than damages for violation of the law. There have been numerous discussions regarding the extent to which equity courts can provide monetary relief.

The Court stated its belief that the district court's concern about the limits of equitable relief was "misplaced" and described theories of equitable relief that might be applied in these circumstances. It emphasized that unlike cases such as *Mertens v. Hewitt Associates*,[6] the relief in this case is sought against a *plan fiduciary* (and not against a nonfiduciary third party), and requested payments from a trust. Claims against trusts are traditionally brought in equity. The Court noted that the power to *reform* contracts to reflect the parties' representations is also a traditional equitable remedy (in contrast to a rewriting of a *contractual* obligation), which might be available in this case. Similarly, estoppel is a theory used in equity courts and also might be available here, although estoppel usually requires a showing of reliance. In addition, the Court suggested that an order requiring that a trustee pay money might be an equitable remedy of a "surcharge against a trustee." The Court disagreed with CIGNA's argument that actual reliance on the communications had to be shown, noting that a showing of detrimental reliance was not required in equitable proceedings for reformation or surcharge (although it was a condition of certain remedies, such as estoppel).

Having recited its views, the Court then remanded the case to the district court for further consideration of whether equitable remedies might be appropriate. Justices Scalia and Thomas issued a concurring opinion agreeing with the decision that the SPD did not constitute a plan document, but maintaining that it was unnecessary to address whether Section 502(a)(3) equitable remedies were available to participants. They argued that the discussion of equitable remedies should be treated as mere dictum (an expression of the Court's views, but not a binding decision of the Court). Interestingly the concurring opinion also included musings on the theories of equitable relief. Significantly, Justice Scalia's opinion noted that if equitable remedies were considered, it might be necessary for plaintiffs to demonstrate actual reliance or actual financial harm, in contrast to the "harm" of having been provided misleading information, which was considered sufficient by the majority and the district court. The extent to which "harm" must be shown to recover damages may be important as *CIGNA* and future cases resolve the scope of available remedies for misrepresentations.

It may be some time before the opinion in the district court on remand is issued, so the ultimate resolution of the case is still in limbo. It has been suggested, however, that the Supreme Court's discussion of equitable remedies opens the door to a wide variety of possible remedies under ERISA that many legal scholars had thought were unavailable.

Lessons for Employers and Plan Sponsors

What lessons does this case have for employers that sponsor benefit plans and those that administer them? Some might argue that the result in the case was forced by extraordinarily bad facts. CIGNA clearly

neglected to describe certain obvious and material disadvantages of the change—the loss of the early retirement subsidy, the effect of the change on CIGNA, and the fact that some people would not earn benefits for a few years under the new plan formula. CIGNA also resisted apparent requests from employees for more information. What is interesting to remember about this case, however, is that there was no need for the employer to "sell" the change to the employees. CIGNA, like many employers, had the right to amend the plan and change, eliminate, or reduce benefits. Had CIGNA announced the change without attempts to "spin" the aspects of the change or downplay the negative effects, the lawsuit might not have been initiated or it might have been dismissed without any attempts to provide relief. While we do not recommend that employers deliberately set out to irritate their employees in communications or announce plan changes by stating something as blatant as: "we're cutting your benefits—too bad for you," we do recommend that employers resist the quite understandable instincts of professional communication consultants to "emphasize the positive." Those very logical recommendations may not be the best practices in a rather litigious employee benefits world.

Many employers have already learned the lessons of the *CIGNA* case and are careful to be straightforward in any notices communicated when pension benefits are changed. Indeed, as explained above, IRS regulations now explicitly require disclosure of the effect of the changes when a traditional benefit formula is converted to a cash balance plan.

But the lessons of *CIGNA* go beyond cash balance conversions. For example, it is possible that many employers will be changing all or part of the structure of their health plans in response to the recent health reform legislation, the Affordable Care Act. Many of these changes may be seen as positive for participants; but due to cost considerations or other employer concerns, employers may have to make other changes to health plans that are not so well received by employees. While a Section 204(h) notice is not required for health plans (those rules only apply to pension plans), SPDs and summaries of material modifications are required. In addition, group health plans are subject to a new mandate under the Affordable Care Act to provide notice of plan changes 60 days *before* the change takes effect.[7] Many health plan sponsors have a practice of informing participants of prospective changes during open enrollment, which usually occurs before the new coverage period, but the statute will impose additional pressure to ensure that the changes are fully and fairly described. In the health arena, anticipating and explaining all possible ramifications of a change in coverage may be difficult. The *CIGNA* case adds new potential pitfalls for employers grappling with these health plan changes.

Finally, although the Supreme Court held that an SPD is not the plan document, if the district court adopts the Supreme Court's dicta that reformation of the plan to reflect the parties' communications, or money damages under a "surcharge" theory against trust are appropriate

equitable remedies when participants receive inadequate or erroneous information, participants will have powerful new incentives to scrutinize plan communications for errors or misleading information. So despite the Supreme Court's view that its holding was intended to keep SPDs and other communications simple, the result of the *CIGNA* case may be to add legal caveats and explanations to participant communications.

The Department of Labor (DOL) has embraced the Supreme Court's majority view suggesting that equitable remedies for erroneous or misleading communication may be broader than previously understood; the DOL has long argued that monetary relief is an available remedy under ERISA Section 502(a)(3). Indeed, based on the Supreme Court's holding, the DOL immediately filed an *amicus* brief recommending a rehearing of a case decided by the Fourth Circuit Court of Appeals, *McCravy v. Metropolitan Life Insurance Co.*[8] In that case, an insurance company had accepted premiums for life insurance on a child who was older than the plan's stated age limits for coverage. When that child died, and the insurance company reviewed the claim for death benefits, the insurer denied such benefits based on the child's age. The court determined the only available remedy was to return the erroneously paid premiums (and not to pay the death benefit). Whether rehearing is granted and whether the court determines that this case is more like the *Mertens* case (a claim against a nonfiduciary) or the *CIGNA* case remains to be seen.

These developments indicate that the subject of proper ERISA remedies—with respect to both pension and health plans—will be debated in the federal courts over the coming years. While legal scholars are contemplating the more intricate effects of the Court's decision on ERISA remedies and the scope of relief available to plan participants for apparent misrepresentations, at least one lesson is clear—benefits plan communication should not use techniques used on Madison Avenue or by political consultants to sell products or candidates. Rather, any explanation of plan or policy changes should be a straightforward one that accurately reflects both the positive and negative aspects of the change.

Notes

1. 563 U.S. __ (May 10, 2011).

2. 534 F. Supp. 2d 288, 296 (D. Conn. 2008).

3. Under current regulations effective today, so-called 204(h) notices must describe the effect of a plan amendment on early retirement subsidies and contain a description of benefits before and after the amendment, as well as sufficient information for each individual to determine the appropriate magnitude of the reduction. Treas. Reg. § 54.4980F-1, Q/A-11.

4. 559 F. Supp. 2d 192, 195 (D. Conn. 2008).

5. *See* 559 F. Supp. 2d 192, 208 (D. Conn. 2008).

6. 508 U.S. 248 (1998).

7. *See* Public Health Service Act § 2715(d)(4). The effective date of this mandate is not entirely clear. The "modifications" are intended to apply to summaries which will be subject to model disclosure statements that have yet to be released by the applicable government agencies.

8. 2011 U.S. App. LEXIS 9914 (4th Cir. May 16, 2011).