Rights of ownership in the United States as identified through defined benefit plan conversion

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RIGHTS OF OWNERSHIP IN THE UNITED STATES AS IDENTIFIED THROUGH DEFINED BENEFIT PLAN CONVERSION

by

RICHARD E BURKE JR.

A thesis submitted in partial fulfillment of the requirements for the Honors in the Major Program in Accounting in the College of Business Administration and in The Burnett Honors College at the University of Central Florida
Orlando, Florida

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ABSTRACT

Employer provided Qualified Plans (“Qualified Plans”) are the most efficient supplement to Social Security savings and benefits. Given the significance of the benefits provided as well as the short-term Revenue constraints upon the Federal government in the form of substantially protracted tax deferrals, Qualified Plan legislation should maintain a conservative disposition. Incremental legislative action in the right direction will steadily graduate ERISA to its intended purpose. Unfortunately ERISA is a convoluted maze of formalities, definitions, and regulation that are only substantially understood by an expert and have yet to be adequately explained to the public at large.

Recent publications such as Retirement Heist rouse the public’s consciousness of retirement Plans by enumerating perceived abuses by large corporations. These alleged abuses certainly reflect innovative manipulations within the constraints of Qualified Plans. However, my thesis will prove that these “abuses” reflect the United States’ disposition toward the rights of proprietorship regarding the Qualified Plan. The intent of the thesis is to illustrate this disposition through a study of the Amara v. Cigna Corp. case as well as a review of an actual LLC’s defined benefit plan conversion to a cash balance plan. I will compare and contrast the different approaches taken by these two employers and justify the varied success they each experienced in converting their plans. Through this process, the thesis shall draw conclusions on the United States’ dispositions toward ownership of the qualified plan.
ACKNOWLEDGEMENTS

I would like to thank my mother and father for supporting me throughout my life. I would also like to thank my committee—Nancy Klintworth, Andrew Judd, and Benjamin Rockmore—for enabling me to participate and guiding me through the thesis writing process. Thank you to the Gray-Robinson Employee Benefits department for their invaluable expertise; without you guys I could not even dream of learning and writing about something so complex in such a short amount of time. Last but not least I would like to thank Svetlana Kuzminskaya for being so supportive, so patient, and my best friend.
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LIST OF ACRONYMS

AA – Adoption Agreement
DB – Defined Benefit
DC – Defined Contribution
DOL – Department of Labor
HCE – Highly Compensated Employees
IRC – Internal Revenue Code
IRS – Internal Revenue Service
NHCE – Non-Highly Compensated Employees
QDRO – Qualified Domestic Relations Order
SMM – Summary of Material Modification
SPD – Summary Plan Description
PPA – Pension Protection Act of 2006
CHAPTER I: INTRODUCTION

I. Introduction

Employer provided Qualified Plans ("Qualified Plans") are the most efficient supplement to Social Security savings and benefits. An Employer’s access to large mutual funds, capacity to pay administrative fees, and capacity to staff administration for the Plan make Employer provided Plans a serious driving force behind the United States’ future retirement welfare. What separates Employer provided Qualified Plans from Employer provided nonqualified plans is that the former is in compliance with the Employee Retirement Income Security Act ("ERISA") and therefore indirectly benefits from Federal government subsidization through tax deductions and exemptions. This subsidy is provided by establishing a legal tax shelter for the plan and participants (see Appendix B). Employer contributions to participants are immediately tax deductible for the Employer’s company and any contributions by Employees (see appendix B)—often considered deferrals—are excluded from their taxable income (Krass, 2010 §1 p.1). These contributions become Plan Assets and are all invested (unless the Employee elects to direct their own investments provided their Plan permits them to do so) in a trust that is tax exempt under 26 USC 501(a)—which in turn must also be qualified under 26 USC 401(a)—and distributions from the plan are taxable when received by the participant. Distributions are generally made from the plan upon or after the participant’s retirement but Plan documents (see Appendix B) may permit earlier untaxed distributions on account of death, disability, and other exceptions (Krass, 2010 §16 p. 3-4). Further, the gains earned on these investments of Plan Assets are not taxable by the federal government. All taxation in these processes, with exceptions, is limited to distributions to the participants upon their retirement.
Given the significance of the benefits provided as well as the short-term Revenue constraints upon the Federal government in the form of substantially protracted tax deferrals, Qualified Plan legislation should maintain a conservative disposition. Government-subsidized Employer-provided retirement savings are guided from the onset by principles concerning the availability of benefits, the rights of the proprietor, requisiteness of contract, and fidelity toward obligation. The ideal Qualified Plan synthesizes these principles by incentivizing the Employer (see Appendix B) to provide the former two while establishing heavy punitive damages for violating the latter two. Incremental legislative action in the right direction will graduate ERISA toward this ideal. Unfortunately ERISA is a convoluted maze of formalities, definitions, and regulation that are only substantially understood by an expert and have yet to be adequately explained to the public at large. Recent publications such as *Retirement Heist* rouse the public’s consciousness of retirement Plans by enumerating perceived abuses by large corporations. These alleged abuses certainly reflect innovative manipulations within the constraints of Qualified Plans. However, my thesis will prove that these “abuses” reflect the United States’ disposition toward the rights of proprietorship regarding the Qualified Plan. Only a consistent and sincere national disposition toward ownership—as opposed to subjective tactics such as lobbying—would lead that Department of Labor (“DOL”), the Internal Revenue Service (“IRS”) and the federal Courts to permit the actions which are espoused as corporate “abuses” of the Qualified Plan. The rights of proprietorship include a duality of concerns—the Employer and the Employee. While the Employer is dependent upon the Employee to perform the necessary functions of an organization, the Employee depends upon the Employer for compensation. This dependency includes the benefits and options available in a Qualified Plan. While minimum
wages are a non-voluntary mandate nearly unilaterally enforced by the government for the benefit of every Employee, Qualified Plans in contrast are entirely voluntary programs that Employers alone are responsible for engaging and administrating. The fact that qualified retirement plans are implemented by the Employer necessitates a degree of sensitivity on the part of lawmakers to the needs of the Employer. Like any business decision, the decision whether to adopt and maintain a retirement plan must conform to the cost/benefit paradigm. ERISA’s purpose is to reduce the cost to the Employer for providing Employees with retirement benefits in order to, in turn, provide the greatest benefit to society by maximizing participants and their retirement benefits.

Why does an Employer elect to start a Qualified Plan for their company? Qualified Plans are adopted by Employers in order to attract employees, reduce employee turnover, increase employee incentive, and to establish a tax-efficient method of accumulating funds from the company for their retirement (Krass, 2010 §1 p.1). The nonqualified plans can also satisfy the former three but any funds they establish are vulnerable to creditors in the case of a default or bankruptcy; nonqualified Plans can receive funded treatment, but “it usually will have to satisfy the numerous and often burdensome requirements contained in Title I of ERISA, which pertain to participation and vesting, funding, and fiduciary requirements” (Downey, 2010 §1 p. 15-16). This makes a non-qualified Plan significantly less reliable than a Qualified Plan because a Qualified Plan’s investments are held in a spendthrift trust meaning they are not technically part of the Employer or Employee’s assets with respect to the fact that they are inaccessible to creditors (Ferenczy, 2012 §4 p. 3). For a Defined Contribution (“DC”) Plan as well as a Defined Benefit (“DB”) Plan, Employers accumulate funds for their retirement by contributing to the
Plan. However, most people with the leverage to make the decision to adopt a Qualified Plan—all whom would be considered “Employers” pursuant to ERISA—are Highly Compensated Employees (“HCEs”; see Appendix B) that must conform to specific non-discriminatory rules with respect to the Plan. These non-discrimination rules include the requirement that HCEs can only make a contribution or receive a benefit that is at most marginally greater than eligible non-excluded Non-Highly Compensated Employees (“NHCEs”) (Krass, 2010 §27 p. 130-131). The IRS has often ruled against Employers attempting to abuse these provisions by excluding certain classes of otherwise eligible employees from the plan (Krass, 2010 §4 p. 10). For any type of Qualified Plan with NHCEs and HCEs for participants, coverage rules require that “the percentage of NHCEs who benefit under the retirement plan must equal at least 70 percent of the percentage of HCEs” or “the average benefit percentage of NHCEs of the employer must equal at least 70 percent of the average benefit percentage for HCEs of the employer” (Krass, 2010 §5 p. 16, 18). The Employer with a Qualified Plan is incentivized, therefore, to encourage as many eligible NHCEs to participate and contribute the highest percentage of their compensation possible in order to reach the maximum contribution limit as established by the IRS. This Employer may make a discretionary contribution to the Employee’s account for the purpose of raising the percentage of compensation contributed in order to pass non-discrimination testing. This Employer may also include a provision to “match” any Employee contribution with an Employer contribution which in turn acts as an incentive for the participant to contribute, further increasing the percentage of compensation contributed. The employer with a DB plan is similarly incentivized by non-discrimination rules to permit NHCEs to receive a greater benefit upon retirement because that means the HCEs are also permitted to receive this higher benefit. With
the exception of age discrimination, this is the extent to which I will be discussing the non-discriminatory requirements of ERISA. The degree of explanation required would only be marginally beneficial to the thesis and significantly onerous to both the reader as well as the author.

II. Significance of Study

As illustrated, ERISA’s tax benefits promote the Qualified Plan’s adoption by Employers whereas the non-discrimination and coverage rules incentivize the Employer to ensure that as many eligible Employees participate as possible and that they receive a fair percentage of their compensation as a benefit. Therefore, a delicate balance between benefits, flexibility, and regulation is maintained within Qualified Plans established by the current rules in ERISA. Public concerns over these rules in a democratic society will inevitably lead to legislative changes in ERISA as well as non-qualified plans. The quality of these legislative changes will be determined by the dispositions of elected representatives whose outlooks are determined, in turn, by the moods of the voting public. Most of the voting public do not possess adequate context regarding the balance between benefits, flexibility, and regulation that make Qualified Plans attractive to Employers in the first place. Even Employees participating in a Qualified Plan do not possess adequate knowledge regarding this balance—the Summary Plan Description (“SPD”), additional disclosure, and Plan Document available to them only define the terms of the Plan and provide no explanation for the reasons behind these terms. In this platonic cave of forms the only shades of information available to the public at large concerning ERISA’s incentive/regulation balance are from the news media. The degree of deliberation involved in
regulations and court decisions establishing this balance within the voluntary Qualified Plan should receive as much expression as the Employee-oriented journalistic coverage on the matter. I believe the disposition of Qualified Plan ownership in the United States as established through the courts and current industry practices will assist the consistency and statutory health of ERISA and its amendments.

III. Review of the Literature

Industry Guidance Publications

The most essential guidance on Qualified Plan administration comes from Sal Tripodi’s *The ERISA Outline Book*, the BNA’s *Tax Management Portfolios*, and Aspen Publishers’ “Answer Books” on retirement plans. These publications impart a prose interpretation of Qualified Plan regulations as they relate to common and specific administrative inquiries. They often identify legislative ambiguities and promote court, Internal Revenue Service and Department of Labor opinions on the language of regulation. These publications often lack perspective from recent cases of Qualified Plan manipulation which have not been specifically identified as prohibited by regulatory oversight. While it can be reasonably inferred that anything is permitted granted it is not expressly forbidden by previous interpretations of ERISA, guidance from these publications provide insufficient perspective on Employers’ Plan activities that have been carried out unchallenged. The thesis will illustrate an activity that lacks adequate expression in industry guidance. This activity is the replacement of a Defined Benefit Plan with a Cash Balance Plan. Generally, the conversion ultimately reduces the potential future benefit accruals of participants—in apparent contradiction to the anti-cutback rules of IRC §411(d)(6).
The thesis will identify and contextualize this contradiction and then draw conclusions on the United States’ legal disposition toward Qualified Plan ownership.

_Retirement Heist & Other Reports on Qualified Plan Manipulations_

These publications indirectly guide the discussion and intent of this thesis. The conversion of a DB plan to a cash balance plan has been identified by journalists an “abuse” because of the activity’s seemingly contradictory relationship to the legislative intent of ERISA. While industry guidance only reflects the Employer’s perspective, journalism on Qualified Plan “abuses” is highly orientated toward the Employee’s perspective. However, journalists, like the Employees they cover, also lack the technical background to analyze Plan mechanics and therefore suffer from an inability to distinguish where a failure in regulation has occurred, if at all. Further, journalism on these “abuses” does not adequately express the opinions of the IRS and DOL despite that fact that these departments are the most vocal and authoritative specialists on retirement plans in the United States. These articles’ silence on IRS’ and DOL’s opinions and activities is the equivalent of writing an article on prison violence and omitting the actions of the prison guards and the warden. The thesis will illustrate Qualified Plan abuses from a structural and legal perspective and address how the IRS’, Federal Court’s and the DOL’s stance reflects the United States’ broader stance on ownership of the Qualified Plan.

**III. Methods and Procedures**

The Qualified Plan “abuse” I illustrate will be contextualized and ultimately reflect the extent of the Employers’ ownership of the entity and plan given the acts’ legitimacy as granted by Qualified Plan regulators. Concerning the reduction of potential benefits as well as
disclosures to participants I will gather data on an investment agency that shall be deemed Employer X, LLC and how they performed a conversion from a DB plan to a cash balance plan. With this data I will relate the attorney’s guidance and subsequent amendments to the Employers’ sovereignty over the plans. I will also review the recent CIGNA v. Amara cases for further details on the permissibility of cuts in potential benefits. These analyses will culminate into an assessment of the Employer’s right to control the Qualified Plan, particularly the defined benefit plan.

IV. Structure

The thesis will be structured as follows. The objective of Chapter One is to provide background, methods, and the significance of the study. Chapter Two illustrates Employers’ adjustment from a Defined Benefit Plan to a Cash Balance Plan and explores the Employer’s latitude to make cuts in potential benefits. In Chapter Three, final conclusions are drawn concerning the extent of the Employer’s Plan ownership given the permissibility of these Qualified Plan manipulations.
CHAPTER II: THE DEFINED BENEFIT PLAN’S CONVERSION TO A CASH BALANCE PLAN

I. Amara v. Cigna Corp.

a. Overview of Facts

Prior to 1998 CIGNA Corporation ran a defined benefit plan in the form of an annuity based upon the employee’s salary and length of service. The retirement benefit provided to an employee in this plan would either equal (1) 2% of the employee’s average salary over his/her final three years with the employer multiplied by the number of years worked—up to 30—or (2) 1⅔% of his/her average salary over their final five years with the employer multiplied by the number of years worked—up to 35 (CIGNA Corp. v. Amara, 2011). The participants who received the benefit calculated by the first formula were all employees hired before December 31, 1988 and were considered “Tier 1 employees”. The participants that received the benefit calculated by the latter formula were all employees hired after December 31, 1988 and were considered “Tier 2 employees” (Amara v. Cigna Corp., 2008). Both methods calculated in this fashion provide an annual retirement benefit that approaches roughly 60% of an employee’s final salary over time payable only in the form of an annuity. This plan also included an option to receive early retirement benefits at age 55 that provided a larger annuity than the employee would have been received under the aforementioned terms (CIGNA Corp. v. Amara, 2011). After 1998 CIGNA implemented a new plan that creates an individual retirement account for each employee in which the employer contributes an amount equal to between 3% and 8.5% of the employee’s salary depending upon age, length of service, and other factors (see table 1). This account then earns compound interest at a rate equal to the return on 5-year treasury bills the
previous November (Amara v. Cigna Corp., 2008) plus .25% but cannot earn less than 4.5% or more than 9%. The employee receives the amount on his/her individual account upon retirement in either the form of a lump sum or annuity. The retirement benefits employees earned under the former defined benefit plan were each reduced to their present value and contributed to each of the employees’ accounts; this was their 1998 opening balance. Further, the new plan also provided a guarantee that an employee would, upon retirement, receive the greater of the amount in his/her individual account or the benefit he/she was entitled to as of January 1, 1998 (CIGNA Corp. v. Amara, 2011).

Table 1: Credit Rates for CIGNA’s 1998 Cash Balance Plan

<table>
<thead>
<tr>
<th>Age and Service Points</th>
<th>Rate Applied to Pay Up to Integration Level</th>
<th>Rate Applied to Pay Over Integration Level</th>
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<tr>
<td>Under 35</td>
<td>3 %</td>
<td>4.5 %</td>
</tr>
<tr>
<td>35-44</td>
<td>4 %</td>
<td>5.5 %</td>
</tr>
<tr>
<td>45-54</td>
<td>5 %</td>
<td>6.5 %</td>
</tr>
<tr>
<td>55-64</td>
<td>6 %</td>
<td>7.5 %</td>
</tr>
<tr>
<td>65 or More</td>
<td>7 %</td>
<td>8.5 %</td>
</tr>
</tbody>
</table>

For example, an employee aged 40 with ten years of service would have 50 service points. If the employee earning $60,000 in a particular year and had a Social Security integration level of $43,500 then the employee would receive a pay credit of $3,247.50 (5% of $43,500 plus 6.5% of $16,500) (Source: Amara v. Cigna Corp., 2008)

b. Outline of the Cash Balance Plan & Comparison with the Defined Benefit Plan

CIGNA’s Qualified Plan adjustment in 1998 represented a conversion from a traditional defined benefit plan to a cash balance plan. The cash balance design is considered a hybrid plan because it possesses elements characteristic of both defined benefit and defined contribution plans. CIGNA’s cash balance plan design provides the participant a benefit based upon the balance of a hypothetical account attributed to the participant as an individual—a characteristic which bears a resemblance to the defined contribution plan design. Unlike the defined
contribution plan, the individual account is granted pay credits rather than an actual cash allocation. The account is granted pay credits based upon a percentage of the participant’s compensation. In the case of CIGNA’s new plan, participants received annual pay credits between 3% and 8.5% of the employee’s salary depending upon age, length of service, and other factors. Along with these pay credits, cash balance plans also provide the participant with credits representing hypothetical interest that accrue even after a participant is no longer performing services for the employer. In the case of CIGNA’s new plan, the participant’s hypothetical account receives additional interest credits at a rate equal to the return on 5-year US treasury bills the previous November plus .25%—a variable interest rate. CIGNA’s plan also stated that this interest credit rate, given the variability of US treasury bills, could not earn less than 4.5% and could not earn more than 9% (Brown, 2011 p. 37-39).

Compared to traditional defined benefit plans, cash balance plans have a more front-loaded accrual: assuming the same final benefit at retirement under both plans, a participant under a defined benefit plan will earn a majority of his/her benefit within the few years immediately before retirement whereas a participant under a cash balance plan will earn a majority of their benefit over a much broader time period. The front-loaded nature of a cash balance plan’s accrual also means that a participant under a cash balance plan will earn greater benefits in their first years of enrollment than they would have under a defined benefit plan assuming the end benefit was the same. This means that any fully vested participant who terminates employment early will have earned a significantly larger amount under the cash balance plan than they would have under a defined benefit plan (this is still assuming that both of these plans ultimately provide the same benefit to participants after the same number of years of
service). This makes the cash balance design particularly attractive to employees in an industry with relatively high turnover—changing jobs often does not eliminate nearly as much potential benefit accrual as it would if the industry were dominated by traditional defined benefit plans. Conversely, this high-turnover scenario would be less desirable to the employer because earlier termination represents a much greater cost to the employer than it would have under a defined benefit plan (Brown, 2011 p. 37-39). In CIGNA’s case, there was a disparity in the pay-credit rate that granted a greater percentage to an employee of higher age and/or length of service. This permitted disparity offsets the front-loaded aspect of their cash balance plan in order to provide an increasing accrual rate overtime (41).

c. CIGNA’s conversion procedures

In order to execute the conversion from a defined benefit to a cash balance plan CIGNA signed a plan amendment to freeze the benefit accruals of all Tier 2 employees and Tier 1 employees with age plus years of credited service less than 45. The Tier 1 employees with age plus years of service greater than 45 were “grandfathered” into the new plan under the same benefit accrual method and formula used in their old defined benefit plan (Amara v. Cigna Corp., 2008). Because Tier 1 employees by definition had been employed by CIGNA for at least ten years at the time of the defined benefit plan conversion, this means that every Tier 1 employee older than 35 years of age retained their previous defined benefit accrual formula as well as their other benefits under the old plan; every other participant and subsequent new participants began to accrue retirement benefits under the provisions and formulas of the new cash balance plan.
The method from which CIGNA chose to convert their participant’s defined benefit accruals into cash balance plan credits was to establish an “initial opening balance” which would accumulate subsequent annual credits. This conversion is performed by establishing the present value of the participant’s accrued normal retirement benefits using mortality and interest assumptions (Brown, 2011 p. 43-44). Prior to the Pension Protection Act of 2006’s explicit establishment of guidelines concerning this conversion, ERISA had no provisions that established any discount rate to use in order to determine present value for this purpose (Sunder v. U.S. Bancorp Pension Plan, 2009). One of CIGNA’s consultants advised the company that opening balances “could even be zero if you wanted” and that the September 2000 General Accounting Office Report stated “current federal law does not govern how plan sponsors set opening hypothetical account balances for cash balance plans, provided that a plan ensures that participants do not receive less than the present value of prior accrued benefits if they separate from the employer” (General Accounting Office, 2000).

CIGNA calculated the converted participant’s initial balance by taking their accrued annual benefit at normal retirement age and determining the actuarial present value of the benefit based on a 6.05% interest rate and a 1983 (unisex) Group Annuity Morality Table or “GATT Table”. This table discounts the retirement benefit given the likelihood that the participant dies sometime between his/her current age and the normal retirement age of 65. Because the table was used to make a one-time discount instead of updating the balance as the likelihood of death during their employment diminishes, there was no way for participants to recoup this discount overtime. Tier 2 employees whose total age and years of service was greater than 55 had their interest rate adjusted to 5.05% and the accrual was discounted for present value with the
assumption that they would receive the accrual at age 62 instead of 65—this gave older or longer service employees a more favorable initial account balance (Amara v. Cigna Corp., 2008).

CIGNA’s post-1998 plan provision to contribute the present value of benefits already earned under the previous defined benefit plan was not necessary for compliance with the IRS given the fact that the provision to guarantee at least the benefit entitled to the participant as of January 1, 1998 was sufficient to establish the plan’s compliance to IRS Code §411(d)(6) and §204(g) of ERISA. These sections establish that a non-ESOP Qualified Plan is no longer in compliance with the IRS code if it is ever amended in such a fashion that any accrued benefits or optional forms of benefit are reduced or eliminated.

d. The Necessity of Indexing a Future Benefit

CIGNA’s plan conversion resulted in benefit reductions that range from 30% to 50% of potential future benefit accruals (Amara v. Cigna, 2006). This can be explained by the fact that the conversion amendment ultimately adjusted the type of index to which a participant’s final benefit was tied. Defined benefit plans generally base annual retirement benefits upon final pay or average final pay over a brief period of time before normal retirement age. This provision is perceived as a preventative measure to ensure that the future retirement benefit is not eroded by inflation overtime—a particularly deep concern for anyone that plans to save money. However, this is not a true protection from inflation because there is no guarantee that inflation will not exceed the rate of increase in a participant’s pay. It is more accurate to describe the provision as a way to index the participant’s benefit to the participant’s rising standard of living. This
assumes that the participant’s salary always increases, a plan may also provide a benefit based on their highest annual salary or an average of their highest paying years. (Brown, 2011 p. 3).

If the benefit is not tied to final pay but instead indexed to the employee’s average pay over their career then there is a significantly weaker link between retirement benefits and the participant’s steadily increasing standard of living or national inflation. A career average benefits index would be a lot less valuable to a younger employee that works under the same plan until retirement—his/her pay may have increased dramatically but a defined benefit plan accrual defined under these terms would average it out. This is why most defined benefit plans index the accrued benefit to final pay during years of service (Brown, 2011 p. 3).

The act of converting a defined benefit plan to a cash balance plans has been described as a method for businesses with a defined benefit plan to reduce future accrued benefits for employees by effectively adjusting the prior plan’s annual benefit to a much lower benefit. One of the ways this adjustment is made is by adjusting the disposition of the salary that the retirement benefit is based off. This adjustment is from years when the employee received their highest salaries (DB) to the average salary over their career (cash balance). This is because each credit to a participant in a cash balance plan is made on an annual basis and is based upon their compensation and compounded by the interest credit, often indexed against the interest rate on treasury bills (Lofgren, 1986).

e. Wear-away

A controversial technical aspect concerning the conversion of a defined benefit plan to a cash balance plan is the concept of “wear-away”. Wear-away occurs when a participant in a
cash balance plan does not accrue any additional benefits for retirement despite the fact that they are earning credits and accruing interest credit on their account. This credit/benefit disparity arises when a participant’s initial account balance on the cash balance plan is computed by discounting the participant’s earned future annuity into a lump sum using an interest rate higher than the IRC §417(e)(3) rate. This makes the participant’s opening account balance less than the present value of the participant’s benefit already accrued under the defined benefit plan (Brown, 2011 p. 57). The April 13, 1998 issue of Pension and Benefits Week states that “[t]he interest rate used under Code Sec. 417(e)(3) is the annual rate on 30-year Treasury securities for the month before the date of distribution or any other time as prescribed by regulation” (“IRS regs conclusion”, 1998). Another way that wear-away occurs is when the proper IRC §417(e)(3) interest rate is applied to calculate the lump sum but the discounting does not begin at the participant’s early retirement benefit—the participant’s initial balance does not take into account the value of the early retirement subsidy (Brown, 2011 p. 57).

The IRS has endorsed and not explicitly prohibited wear-away. This concept does not violate ERISA §204(g) prohibiting amendments that allow accrued benefits or optional forms of benefit to be reduced or eliminated because the concept by definition indicates that an already accrued benefit has not been reduced or eliminated. Plan language that guarantees the participant receives the greater of his/her accrued defined benefit under a previous plan or account balance under cash balance plan is sufficient to indicate to the participant and to the IRS that an accrued benefit has not been reduced. Previous permutations of wear-away have already been approved by the IRS as an acceptable method employers could use to change the terms of their defined benefit plan. This concept previously applied to a change in actuarial factors wherein a period of
wear-away resulted from the fact that the benefit accrued under the previous actuarial factors was greater. Another instance of the IRS’ endorsement of wear-away was after the enactment of the Tax Reform Act of 1986 where most defined benefit plans at the time were required to change some elements of their plan formula or design. To assist employers, the regulations described three approaches that employers could use to transition the defined benefit plans into compliance with the new law. The three different pre-approved methods were described as “fresh start without wear-away”, “fresh start with wear-away”, and “fresh start with extended wear-away”.

In a generic sense, when a plan has a provision that includes a minimum benefit formula that is a fixed dollar amount or fixed percentage of compensation and a participant in that plan has greater minimum benefits than he does benefits under the increasing accruals of the plan’s main benefit formula, that participant is experiencing wear-away (Brown, 2011 p. 57-58). CIGNA’s use of interest rates higher than the return on 5-year treasury bills from the previous November and the irrecoverable mortality discount on calculating initial account balance made their plan participants experience wear away on their benefits.

Documents for participants disclosing CIGNA’s conversion from a defined benefit plan to a cash balance plan were distributed on December 1997. Four versions of this disclosure were distributed to four different types of participants—those switching to the cash balance plan, those who maintained the provisions under the previous defined benefit plan, and those that did either and also participated in CIGNA’s supplemental pension plan. These disclosures included details on how the defined benefit accrual was converted into an initial balance on the individual’s cash balance plan account—present value of the annuity benefit assuming a 6.5% interest rate, 5.5% interest rate and briefer period for participants with greater than 55 service credits, etc.— but did
not mention the pre-mortality discount that was applied. A heading in the statement asks the question “Will my benefit be better under the new Retirement Plan?” which is answered by the statement that “…exact comparisons of benefits that cover all possible outcomes are difficult…[the plan] tends to provide larger benefits for shorter-service employees and comparable benefits for longer-service employees…” The statement includes no discussion concerning the wear-away inflicted upon all participants caused by both the use of the GATT table to discount for mortality as well as higher assumed interest rates. The 1998 Summary Plan Description also did not explain wear-away but did mention the plan’s minimum benefit rule (Amara v. Cigna Corp., 2008).

f. Claims Against CIGNA Regarding Age Discrimination

Mrs. Amara filed a class action lawsuit against CIGNA Corp. Their chief argument was that CIGNA’s cash balance plan violated the age discrimination provisions of the Internal Revenue Code (“IRC”) and ERISA. IRC § 623(i)(1)(A) states that “it shall be unlawful for an employer, an employment agency, a labor organization, or any combination thereof to establish or maintain an employee pension benefit plan which requires or permits in the case of a defined benefit plan, the cessation of an employee’s benefit accrual, or the reduction of the rate of an employee’s benefit accrual, because of age.” CIGNA’s expert on retirement claimed that if the rate of interest accrual and accrual of pay credits does not violate age discrimination—older, longer-serving employees accrue the same or higher pay credits as younger and/or shorter-serving employees. Further, participant’s defined benefit accrual/initial cash balance conversion even granted a favorable rate to older/longer service participants. While CIGNA claims that the
rate of benefit accrual determines age discrimination, Amara’s class contends that the ultimate benefit upon retirement determines whether a Qualified Plan is committing age discrimination. Their retirement expert stated that a younger worker would receive a greater annuity upon retirement than a similarly situated older worker with the same service record and compensation because the younger worker would receive more annual account credits and benefit from compound interest (Amara v. Cigna Corp., 2008). A United States 7th Circuit Court of Appeals judge stated in Kathi Cooper v. IBM Personal Pension Plan that the plaintiff’s argument “treats the time value of money as age discrimination” and that when an accrued benefit is properly discounted for time value the interest credit benefit disappears (Kathi Cooper v. IBM Personal Pension Plan, 2006). The Amara v. CIGNA court of 2008 agreed with this sentiment and ruled that CIGNA’s cash balance plan is not age discriminatory. It also addressed the plaintiff’s argument that the degree of wear-away for older participants was far greater than it was for younger participants. The plaintiff cited the fact that the calculation of initial account balance did not take into account the early retirement benefits. CIGNA’s experts testified that wear away was principally driven by the fall of interest rates during the time the initial account was calculated (Amara v. Cigna Corp., 2008). The court also agreed with the District of Connecticut judge in Custer v. Southern New England Telephone Company that “The ‘wear-away’ period is not necessarily longer for older workers; it is longer for workers that have greater frozen benefits. Under the old plan, the size of a worker's frozen benefits is a function of a worker's salary and years of service, not his age… Because a workers' [sic] frozen benefits are not a function of the worker's age, the size of the ‘wear-away effect’ is not a function of the worker's age” (Custer v. S. New Eng. Tel. Co., 2008). The plaintiff’s expert conceded that the GATT table discount
created greater wear-away for younger participant’s than older. The Amara v. Cigna Corp court concluded that the plaintiff’s charge of age discrimination was simply based of their perception of a plan’s transition from a plan that heavily favored older, longer-service participants to a plan that was still favored older, longer-service participants “but less so” (Amara v. Cigna Corp., 2008).

g. CIGNA’s Denial of Liability

The plaintiffs in Amara v. Cigna Corp. also claim that CIGNA did not provide required disclosures to employees and that the disclosures CIGNA provided did not meet the statutory standards under ERISA. CIGNA, however, claimed that the plaintiffs had not sued the right defendant with respect to these claims. They argued that the plaintiff’s failure to name the plan administrator (see Appendix B) as a defendant—in addition to CIGNA and the CIGNA pension plan—preempts their claims regarding plan documents and disclosures because only the plan administrator is liable for any defects in notices and disclosure that are required for Qualified Plans under ERISA. The court acknowledged that this facet of ERISA law remains relatively unclear, even in case law. The aforementioned Custer v. Southern New England Telephone Company only named the plan and the employer as defendants but had not discussed the possibility that only the plan administrator could have been held liable for failures within the plan document and disclosures. In Richards v. Fleetboston Financial Corp. (427 F. Supp. 2d 150), the court dismissed claims against the employer when relief was requested under ERISA §502(a)(1)(b) allowing civil action to be brought “to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future
benefits under the terms of the plan” but allowed claims against the employer when relief was requested under ERISA §502(a)(3) allowing civil action to be brought “by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of [ERISA] formally “this subchapter” or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of [ERISA] same or the terms of the plan”. This case distinguishes under what statutory sections of ERISA the participant could seek relief from the employer but does not establish whether the plan administrator could be the sole person held liable for defects in required notices and disclosures (Amara v. CIGNA Corp., 2008).

The only defendants named in this case were CIGNA and the CIGNA Pension Plan. CIGNA’s claim that the plan administrator is the only person liable for defects in required disclosure is based on explicit language in ERISA that requires the plan administrator to provide these disclosures. The Second Circuit has previously permitted suits attempting to recover plan benefits to proceed against the administrator of the plan and/or the plan itself while limiting inadequate disclosure claims solely to the plan administrator (Amara v. Cigna Corp., 2008). A US Second Circuit Court of Appeals claimed that “ERISA undoubtedly requires that participants be told who has the financial obligation to fund the plans. But that obligation is placed on the person designated under ERISA as the ‘administrator’ of the plan, not on every fiduciary” (Lee v. Burkhart, 1993). Also, a US Seventh Circuit Court of Appeals claimed that “Western General, the only defendant, cannot be held liable for any inaccuracies in the SPD. Congress has explicitly provided that the responsibility for complying with these statutory requirements falls on the plan administrator. The case law also confirms that
any cause of action for violations of these disclosure requirements is proper only against the plan administrator, the party responsible under the statute” (Klosterman v. Western General Management, 1994).

Amara’s class responded to CIGNA’s argument by stating that the two plan administrators were not effectively designated to be plan administrators by CIGNA—making CIGNA the plan administrator by default—and that even if he was a valid plan administrator the effective control over the content and delivery of the defective plan documents and disclosures remained with CIGNA and therefore CIGNA should be held liable for these defects. The plaintiffs claimed that CIGNA had not effectively established a plan administrator because—citing U.S.C. §1002(16)(A) that a plan “administrator” is the plan sponsor if an administrator is not designated under the terms of the plan—the cash balance plan document did not designate any named individual as plan administrator. However, the Code of Federal Regulations title 26 §1.414(g)-1(a) states that a plan document may designate a plan administrator “[b]y reference to a procedure established under the terms of the instrument pursuant to which a plan administrator is designated”. The Amara v. CIGNA Corp. court found that CIGNA’s plan used this method—Article XIII called “Plan Administration” states: “[t]he [Corporate Benefit Plan] Committee shall delegate to a Plan Administrator the duties, authority and functions set forth in this Article XIII” and that “[t]he Plan Administrator shall perform all such duties as are necessary to operate, administer and manage the Plan in accordance with … its terms…”. The court rejected the plaintiff’s argument claiming that the plan administrator was not validly appointed but agreed with the plaintiff’s claim that CIGNA should be treated as the effective administrator of the Plan for purposes of the defective disclosures. This was because CIGNA alone prepared and
published the disclosures—the plan administrator was so peripheral that he was not even on CIGNA’s list of likely witnesses at trial. Instead, a former Vice President was chosen to testify regarding “[c]ommunications about the conversion to [the cash balance plan] and the operation of [the cash balance plan]”. Additionally, the initial newsletter sent to participants announcing the plan conversion entitled “Introducing Your New Retirement Program” was published by CIGNA Benefits Communications, the plan administrator’s name was not mentioned anywhere in the newsletter, and the newsletter informs readers, “If you have questions, please e-mail your questions to Signature Benefits Services…or you may call Signature Benefits Services…” There was no indication that the plan administrator was in any way involved in the preparation or dissemination of the Summary Plan Descriptions though these were in fact the first documents that indicated to participants that they should contact the plan administrator regarding any questions they have concerning the new plan. The Amara v. CIGNA Corp. court also found that it appeared that CIGNA as an entity—rather than the plan administrator—sought out William Mercer—a consulting firm—for assistance in preparing the required disclosures for their plan transition. CIGNA argued that the Second Circuit Court of Appeals had previously held in Crocco v. Xerox that lawsuits to recover benefits under §502(a)(1)(B) (see above) can only be against “the plan administrators and trustees of the plan in their capacity as such” and that an employer may not be considered a de facto co-administrator of a plan qualified under ERISA. The Amara v. CIGNA Corp. court felt that Crocco was judged a case with circumstances disparate from the CIGNA case. Crocco involved a participant’s claim for plan benefits that the plan administrator herself denied—the company was in no way involved other than in its capacity as the employer of the plan administrator. In Amara’s case the employer, not even the plan
administrator, possessed full control over the processes alleged to have violated ERISA—the issuance of notices and disclosures are qualitatively different than a plan administrator’s denial of a participant’s claim to plan benefits. Despite this, the plain language of Crocco’s judgment prevented the Amara v. CIGNA Corp. court from finding CIGNA liable for inadequate disclosures under 502(a)(1)(B) even if they are considered the effective co-administrator of their cash balance plan. However, this did not exempt them from being liable for claims against an employer on behalf of the plan for a breach of fiduciary (see Appendix B) duty under §502(a)(2) or claims for injunctive or other equitable relief under §502(a)(3) and the court held that the plaintiffs were permitted to pursue their defective disclosure claims against CIGNA under the latter statute (Amara v. Cigna Corp, 2008).

h. Overview of ERISA’s Required Disclosures to Participants

SPD & SMM

ERISA requires Qualified Plans to disclose key information about the plan and its operation to participants and their beneficiaries; employers that are not in compliance with these disclosure requirements may face penalties. The following documents are required to be distributed to participants and beneficiaries: (1) the summary annual report, (2) the summary plan description (“SPD”), (3) the summary of material modification (“SMM”), (4) a statements of benefits to terminated vested employees, and (5) a notice of failure to meet minimum funding standards. The Department of Labor suggests these disclosures be distributed in-hand to an employee at his/her worksite—it is not acceptable to merely place the materials at a location frequented by the plan participants. It is permitted for the employer to distribute required
disclosures in a periodical that is distributed to employees (e.g. a publication in a union newspaper or a company publication) provided that distribution is all-inclusive and a clear notice on the front page informs readers that the publication contains important information about the rights granted under the plan and ERISA and should be read and kept for future reference. Because participants and beneficiaries may not receive these periodicals, they often must be supplemented by other authorized distribution methods calculated to ensure actual receipt (Kushner, 2011 p. 57).

A Summary Plan Description (“SPD”) is a written summary of the Qualified Plan’s contents; DOL regulations specify its required contents. ERISA requires that the SPD be written with the intent to be easily understood by the participant or beneficiary. It must be accurate and comprehensively explain to the participants their obligations and rights under the plan. The SPD must also include clarifying examples and illustrations of the more complex aspects within the Qualified Plan. The SPD should never be contradictory to the language within the plan document: a disclaimer is typically included in an SPD stating that the terms of the plan document will govern in the event of a contradiction but courts have been known to hold the employer accountable for SPD language regardless of this disclaimer. There are no monetary penalties for a failure to distribute an SPD per se; there are no monetary penalties for any technical violations of ERISA within the SPD per se. However, there are penalties imposed for either of these violations of ERISA if they are under exceptional circumstances such as bad faith, active concealment, or fraud—ERISA does not provide applicable remedies for these violations (59-60). Title 29 of the Code of Federal Regulations §2520.102-2(a) states that the format of the SPD must not have the effect of “misleading, misinforming, or failing to inform participants and
beneficiaries” and that “[a]ny description of exception, limitations, reductions, and other restrictions of plan benefits shall not be minimized, rendered obscure, or otherwise made to appear unimportant”. Further, “[t]he advantages and disadvantages of the plan shall be presented without either exaggerating the benefits or minimizing the limitations”. A different SPD for each group/class of participants under the plan is permitted. An SPD must be distributed to participants and beneficiaries within 120 days of the date the plan becomes subject to ERISA’s reporting and disclosure requirements—this is the first day that an employee is credited with an hour of service under the plan, the effective date of a plan implemented prospectively, or the SPD must be distributed within 120 days beginning the day after the adoption date of a plan implemented retrospectively. It must also be distributed to a new participant within 90 days after he/she becomes a participant and it must be distributed to a beneficiary within 90 days after he/she first receives benefits form the plan. An updated SPD must be prepared and distributed every 5 years if there have been any amendments to the plan within this time period and a restated SPD must be prepared and distributed every ten years even if no amendments have been made within the past ten years (62-64).

The SPD must include:

1. The plan name
2. The names and addresses of the employer or the employee organization
3. The plan year
4. The list of plan sponsors
5. The EIN and plan number
6. The plan type
7. How the plan is administered
8. Requirements for eligibility
9. The circumstances resulting in the disqualification of benefits
10. Collective bargaining agreements (if applicable)
11. A statement of the participant’s rights under ERISA
12. A summary of the employer’s authority to terminate or amend the plan
13. A summary of any plan provisions governing the allocation and disposition of plan assets upon termination
14. Fees and charges
15. The claims procedure
16. Normal retirement age under the plan
17. Any rights to self-direct investments
18. Joint and survivor benefits
19. The plan’s procedures governing Qualified Domestic Relations Orders (“QDRO”; see Appendix B)
20. How the plan calculates years of service
21. Disclosure regarding—upon a plan merger—any rights under both the successor plan and the former merged plan

With respect to the type of plan that must be described, examples of a plan "type" include a profit sharing plan, a cash balance plan, a defined benefit plan, etc. In describing the plan type the SPD must also illustrate the means by which the plan accumulates funds to pay benefits. The SPD must also explain the sources of contributions to the plan—employer contributions,
employee contributions, matching contributions—and the methods used to calculate the amount of the contributions (64-66).

When a material amendment or other change is made to a Qualified Plan subject to ERISA the plan sponsor must prepare and distribute a Summary of Material Modification (“SMM”) which is an addendum to the plan’s SPD. A restated SPD that includes the necessary amendatory information would also satisfy this requirement. According to the DOL regulation §2520.104b-3(a) the SMM must be distributed to all participants and beneficiaries receiving benefits under the plan within 210 days after the end of the plan year in which the modification was adopted. The SMM must also be distributed to new participants within 90 days of the date they become participants. The SMM must be prepared in a manner intended to be understood by the average plan participant. The general format and distribution requirements of an SMM are the same as they are in an SPD (68).

204(h) Notice

For defined benefit plans ERISA §204(h) requires advanced disclosure of amendments that would significantly reduce the rate of future benefit accrual. This requirement also applies to an individual account plan subject to minimum funding standards—this includes cash balance plans. Because an amendment that reduces early retirement benefits or reduces a retirement-type subsidy is technically treated as reducing future benefit accruals, these amendments by the employer would also require the distribution of a notice to maintain compliance with ERISA §204(h). An amendment that reduces early retirement benefits or retirement-type subsidies is not considered significant if the amendment is intended to be a reduction of benefits that would
otherwise create significant burdens for the plan and participants unless the amendment adversely affects participant’s rights in a greater than minimal degree (72). If the §204(h) notice is not required to be distributed to an employee or alternate payee (see Appendix B) at the time of the amendment, the notice is never required to be provided even if their benefits end up being reduced by the amendment at some point of time in the future (Amara v. Cigna Corp., 2011). A notice intended to remain in compliance with ERISA §204(h) must be distributed within a reasonable time before the amendment’s effective date. It must be distributed to each participant, each beneficiary that is an alternate payee under a QDRO, each employee organization that is representing the participant in the plan, and each employer with an obligation to contribute to the plan. This notice must also be expressed in a manner wherein it can be understood by the average plan participant. It must also contain enough information to allow participants to understand the effect the amendment has upon their benefits. A failure to provide this disclosure will result in an excise tax and an egregious failure to provide this disclosure will result in an invalidation of the amendment for individuals that would receive greater benefits under the plan if the amendment had not occurred. A failure to provide the disclosure is egregious if it is within the control of the plan sponsor and is an intentional failure. The failure is also egregious if it fails to provide most individuals with most of the information they are entitled to receive. An intentional failure can include any failure to provide the notice after the plan administrator discovers the unintentional failure. If the notice is for a defined benefit plan the notice must compare the value of the annual benefit starting at normal retirement age under the amended plan with the value of this benefit prior to the plan amendment. For an individual account plan subject to minimum funding standards the value of benefit to be allocated to the participant’s account in the future under the
amended plan must be compared with this sort of future allocation as it would have occurred 
under the plan had it not been amended. If the amendment is intended to simply comply with 
changes in applicable law then the IRS may waive the §204(h) notice requirement on a case-by-
case basis. The 204(h) notice must be prepared for:

1. Participants or alternate payees whose rate of future benefit accrual is reasonably 
   expected to be significantly less than it was prior to the amendment.

2. Employee organizations that represent at least two participants entitled to receive the 
   notice.

3. All employers obligated to contribute to the plan.

4. The individuals that are reasonably expected to become participants or alternate 
   payees (Kushner, 2011 p. 72-76).

The notice generally must be provided at least 45 days before the amendment’s effective 
date and at least 15 days if there are less than 100 participants with accrued benefits. The 204(h) 
notice must be distributed even if the participant can choose between a benefit formula in effect 
before the amendment and a benefit formula in effect after the amendment. The notice must be 
written in a fashion calculated to be understood by the average participant and include enough 
information to allow participants to understand the impact of the plan amendment. The 204(h) 
notice must also express to the reader the significance of the information it is intended to discuss. 
It must also not contain information that could be considered materially false or misleading; it 
must not omit information that would cause the included information to be misleading. The 
notice must be in narrative form, include the effective date, and describe the benefit allocation 
prior to the amendment’s effective date as well as the benefit allocation after the amendment’s
effective date. If the amendment reduces an early retirement benefit or retirement-type subsidy then the notice must also provide the same type of before/after explanation. The notice must also provide enough information wherein the reader understands the approximate magnitude of the expected future benefit accrual reduction. Examples must be included because it is unreasonable to expect that the recipient would understand the approximate magnitude of reduction simply based on a description of the amendment (Kushner, 2011 p. 72-76) However, according an Internal Revenue Service treasury regulations 1.411(d)-6 Q&A, “[t]he summary need not explain how the individual benefit of each participant or alternate payee will be affected by the amendment”.

i. Claims Against CIGNA Regarding Inadequate and Misleading Disclosure

*The 204(h) Notice & Wear-away*

The plaintiffs in Amara v. Cigna Corp. claimed that CIGNA, as plan administrator, did not comply with ERISA’s statutory and regulatory notice requirements. They claimed that the disclosures included defects in form as well as substance and argue that as a result some aspects of the new cash balance plan were invalid. They also claim that the reason CIGNA provided inadequate notices and disclosures was because they were attempting to intentionally avoid negative employee reactions to the new cash balance plan. CIGNA asserted that it provided all required disclosures and that they were not materially misleading. The specific publications were a November 1997 Signature Benefits Newsletter that CIGNA identified as a §204(h) notice, the December 1997 Retirement Program Information Kit that CIGNA identified as a Summary of Material Modification, the October 1998 Summary Plan Description for the new cash balance
plan, and the September 1999 Summary Plan Description for the cash balance plan. The plaintiff’s claim against the §204(h) notice was that it was deficient because it failed to inform participants that there was a significant reduction in the rate of future benefit accrual due to the conversion from the defined benefit plan to the cash balance plan. They also claim that the Summary Plan Descriptions and the Summary of Material Modification were not adequate because they did not inform participants about the potential of accrued benefit wear-away and that benefits accrued under the defined benefit plan may not have been fully protected.

The required content of the §204(h) notice as it existed prior to 2001 required only a summary of the amendment and the effective date. It was also permissible to substitute the amendment’s summary with the actual text of the amendment so long as it was written to be understood by the average participant. CIGNA argued that the need for a §204(h) notice was not required because the new cash balance plan did not cause a significant reduction in participants’ benefit accrual. This is because the accrual of benefits under the defined benefit plan were frozen since December 31, 1997 and the cash balance plan was not established under December 21, 1998—the notice regarding the freeze—the §204(h) notice—was provided in the November 1997 Newsletter. They argue that no subsequent notice was necessary despite the implementation of the new cash balance plan because any future accrual under the cash balance plan was necessarily the same or greater than the participants’ lack of accrual under the freeze.

The court did not find this argument persuasive despite the fact that the resumption of benefit accrual after the freeze would normally cause an increase, rather than a decrease in participants’ accrual. This is because the freeze was simply an interim phase—CIGNA always intended to establish the cash balance plan subsequently. The newsletter that CIGNA claimed was intended
to comply with 204(h) requirements even stated that the freeze was only an interim stopgap for the new retirement program—the first line of this newsletter reads, “On January 1, 1998, CIGNA will introduce a new retirement program” and it later states that CIGNA will “formally adopt” the new retirement plan on April 1998, retroactive to January 1, 1998. With respect to the initial account balance CIGNA merely states in this newsletter that, “Once [opening] balances are calculated, they will be credited to Retirement Plan accounts retroactively to January 1, 1998, so you won’t lose any interest credits for the first part of 1998” (Amara v. Cigna Corp., 2008). In a different case in the same district the judge noted that “[i]t is not so obvious to this Court that when there is a freeze in benefits, along with the promise of retroactive benefit accruals once the new Plan is adopted, any additional benefit accruals at all constitute an overall increase because the baseline is zero” (Brody v. Enhance Reinsurance Co. Pension Plan, 2003). The Amara v. Cigna court related this position for its applicability to ERISA’s notice requirements because the court considered this portion of ERISA’s purpose to be to “protect employees’ interests and their reasonable expectations”. They felt that if employers were permitted to avoid proper notice requirements simply by exploiting the technicality of freezing previous plan benefits before instituting new ones retroactively then they would be effectively permitted to perform an activity that runs diametrically opposite the legislative intent of ERISA’s disclosure requirements (Amara v. Cigna Corp., 2008).

CIGNA also claimed that the §204(h) notice was not required because the cash balance plan was implemented retroactively—the notice was legally intended to provide a warning to participants regarding prospective changes to their retirement plan. The §204(h) statute requires that the notice be published and distributed “after the adoption of the plan amendment and not
less than 15 days before the effective date of the plan amendment”. They argued that literal compliance with this statute in the case of a retroactive amendment would be difficult, if not impossible. The court disagreed with this notion that the retroactivity of the amendment instituting a cash balance plan invalidates the requirement to distribute a §204(h) notice. It felt that the primary purpose of the §204(h) notice was to provide employees with the opportunity to understand the changes being made to their retirement plan and to possibly protest or otherwise seek to alter these changes if they happen to be unacceptable. It also felt that if CIGNA had provided notice before the retroactive implementation of the cash balance plan then the participants would have had advance notice of the changes—ERISA’s intent regarding disclosure. The Amara v. CIGNA Corp. court found that the retroactive nature of the cash balance plan’s adoption alone was not a sufficient reason to void ERISA’s requirements to issue a §204(h) notice (Amara v. Cigna Corp., 2008).

The court compared the future potential benefit accruals under the defined benefit plan with the future potential benefit accruals under the cash balance plan and found that a significant reduction had occurred. CIGNA itself admitted that if they had “never adopted the cash balance plan…[participants] would have a larger benefit than they have under th[e] conversion”. The plaintiffs’ expert testified that switching from the defined benefit plan with accruals indexed to final or highest average salary to a formula that results in being tied to career average pay will be almost guaranteed to cause a substantial reduction in future accrued benefits. This is generally true because employee salaries typically increase over time and switching from a final average to a career average will necessarily affect future benefit accrual negatively. It was estimated that the defined benefit plan accrual rate was 1.5% of the participant’s highest compensation; the accrual
rate under the cash balance plan, assuming a 4.5% annual salary increase, was approximately
.75% of the participant’s highest compensation. This would mean that CIGNA’s new cash
balance had opening account balances with potentially large periods of wear-away, significantly
lower rate of accrual—when indexed based upon final pay—compared to the defined benefit
plan and a lower interest-credit benefit accrual because the participant would receive fewer
interest credits from having a lower and slower-growing corpus. For example, one participant at
55 had a projected pension benefit of $1.8 million under the defined benefit plan assuming he
had earned a salary that increased by 2% each year. The projected benefit of this participant at 55
with a salary increase of 2% each year would been equal to $1 million under the cash balance
plan. He had a 45% reduction in his benefits. Another participant, one of the few participants that
had been shown an actual comparison of benefits found that even with an unrealistically high
interest credit rate his future benefits were still 29% lower than those he would have received
under the defined benefit plan; using a 5.8% interest credit rate his benefits were reduced by
44%. The Amara v. Cigna Corp. court held that a 204(h) notice was required to be distributed to
participants (Amara v. Cigna Corp., 2008).

ERISA had not required certain elements of disclosure in §204(h) notices prior to 1998.
Since 1998, disclosure of wear-away became a requirement. CIGNA argued that at the time the
cash balance plan was established it was not required to explain the nature or extent of the
reductions themselves or even make any indication that the notice was intended to comply with
§204(h). The plaintiff asserted that these disclosures required a statement to the effect that “your
benefits may be reduced”, that the statement given was not in compliance with Treasury
Regulations 1.411(d)-6 in that it was not “written in a manner calculated to be understood by the
average plan participant”, that the statement should have included some explanation of wear-away, and that the other ways in which benefits were reduced should have been disclosed. They argued that it was unrealistic for CIGNA to believe that a mere summary of the cash balance plan would be comprehensible without explicit acknowledgement of the potential for reductions and the various ways they might occur. The court held that even though the §204(h) statute had not required the additional information, CIGNA’s was still in violation of §204(h) because they had avoided providing such information and they instead offered material misrepresentations suggesting that there had been benefit increases instead. The 2008 Amara v. Cigna Corp. court confirmed from the plaintiff’s attorney that there was nothing in CIGNA’s disclosures that would give anybody any the notion that they may be subject to wear-away. The court found that CIGNA offered statements that misled participants into believing that there would be no component of the new cash balance plan that would result in significant reductions in the rate of future benefit accruals. The 1997 notice stated that “CIGNA will significantly enhance its retirement program” and that “[o]ne advantage the company will not get from the retirement program changes is cost saving”—nothing in this newsletter indicated that participants’ rate of benefit accrual might decrease by a significant margin. This information was equally nonexistent in their other publications regarding the new Qualified Plan. One of its Q&As states that CIGNA “is not reducing the overall amount it contributes for retirement benefits, nor has the new program been designed to save money”. This may me true: the contribution for retirement benefits, given the structure of a Qualified Plan subject to minimum funding standards, would only theoretically and not necessarily be reduced if there were a major decrease in future participants’ benefit accrual. Further, CIGNA argued that this statement was not materially
misleading because they contributed to the 401(k) established alongside the cash balance plan and these contributions counterbalanced any savings they made from the implementation of the cash balance plan. The plaintiffs noted, however, that a portion of CIGNA’s additional contributions to the 401(k) were solely discretionary on the part of the employer—they were allocated only to accounts chosen by CIGNA. The plaintiff’s expert stated that the inclusion of a purported contribution offset to a separate 401(k) plan was not conducive to an accurate and informative disclosure in compliance with ERISA. Further, analysis by Mercer indicated that for benefits to be properly offset by contributions to the separate 401(k) plan CIGNA would have had to provide the maximum discretionary contribution each year and these investments would have had to earn a 9% return each year. CIGNA admitted that the Tier 1 employees with age plus years of service greater than 45 were “grandfathered” into the new plan because “[t]hese employees couldn’t match this benefit growth under the new plan” but they reassured participants in their publications that “[o]ther employees and all new hires will be able to earn comparable benefits as career employees under the CIGNA Retirement Plan”. With respect to the participants that were hired before December 31, 1988 but did not accumulate enough age/service credits to have their old defined benefit plan formula grandfathered in under the new plan, CIGNA also stated in their disclosures, “Our analysis showed that, in comparison to people with a higher age and service combination, you have plenty of time to take full advantage of the many attractive features of the Retirement Plan, plus you will have access to the new lump sum payment option”. Later it says, “The new Retirement Plan is different from the current Pension Plan, so exact comparisons of benefits that cover all possible outcomes are difficult. Generally speaking, the new Retirement Plan, in comparison with the current Pension Plan, tends to
provide larger benefits for shorter-service employees and comparable benefits for longer-service employees.” It also lauded the value of the lump-sum distribution option—a feature unavailable in the previous defined benefit plan—and reassured participants that “[e]ach dollar’s worth of credits is a dollar of retirement benefits payable to you after you are vested (see Appendix B). Under the plan, your benefit will grow steadily throughout your career as credits are added to your account.” The SPD contained similar statements. CIGNA’s retirement kit also included a statement assuring its employees that “[t]he conversion factors we are using to determine your opening account balance are based on guidelines established by the government to ensure a fair transition for employees” and on their SPD it states, “The conversion formula used is based on guidelines established by the federal government for valuing pension benefits”. CIGNA admitted in court that these guidelines do not exist: citing a Government Accountability Office (“GAO”) report on conversions from defined benefit to cash balance plan CIGNA stated that “There is no provision of law that sets forth minimum requirements for determining opening balances.” CIGNA claimed that the disclosures it provided its participants regarding the opening account balances under the cash balance plan as well as subsequent account statements and compensation reports constituted adequate disclosure regarding all material aspects of the plan, thus any deficiencies in the initial plan notices were legally negligible. The court disagreed with CIGNA’s claim that accurate and relevant disclosures negate the fact that they provided defective notices previously. It found that the volume of information they chose to disclose was not relevant to the matter; what was relevant was the statements made that were not written in a manner calculated to be understood by the average participant and failed to provide important details that reasonable employees would have wanted to know regarding the transition from a defined
benefit plan to a cash balance plan. The court found that CIGNA’s adequate explanation of how opening account balances were established did not in of itself provide sufficient scrutable information concerning the transition and could not counteract the favorable impression on the new plan made by CIGNA’s other statements concerning positive features and how participant’s benefits will grow. This would not cure the substantial amount of misinformation contained in CIGNA’s plan and amendment disclosures (Amara v. Cigna Corp., 2008). In a very similar case—what would become Lonecke v. Citigroup Pension Plan—the United States District Court for the Southern District of New York stated that the

   [p]laintiffs had every reason to expect that under the new cash balance plan, their pension would continue to accrue at a rate approved by congress. It therefore had every reason to expect that under the new cash balance plan, their pensions would continue to accrue at a rate approved by Congress. It therefore is immaterial that the December 1999 §204(h) notice stated in bolded font that the 2000 CBA could result in a reduction of their benefits. Given the material omissions, it remained ‘insufficiently accurate and comprehensive to reasonably apprise participants and beneficiaries of their rights’” (In re Citigroup Pension, 2006).

In another similar case another judge in the Southern District of New York stated that “"A notice is intended to give fair warning, and fails to do so if it is cryptic, or requires research beyond the document itself" (Hirt v. Equitable Retirement Plan, 2006).

   CIGNA asked some of its managers to review the cash balance plan and they sent CIGNA a statement that recommended the employer “[p]ublish case studies (positive and negative) and expect to be able to support employees who will be negatively impacted ASAP”.

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They also insisted CIGNA “[s]how illustrations that ‘prove’ small lump sums will yield equivalent benefits in the future (a lot of disbelief among managers about the way we handle data)” and that “[g]eneral reaction to HR support is bad—too many examples of how poor the communications from HR have been in the past; low degree of reliance on information from the division”. These suggestions were ignored by CIGNA. The employer provided a questionnaire attached to its December 1998 Retirement Kit asking, “What additional information would you like CIGNA to provide?” responses included: “More specific detail re: calculation of lump sum”, “…plug in the individual employee’s actual percentage, salary and points making the same general assumptions and project the retirement under the old and new plan”, “Comparison to old pension plan i.e. dollar amount i.e. would lump sum distribution buy an annuity comparable to old pension plan?”. Despite these requests by employers and CIGNA’s sufficient knowledge on the true effects on participants’ rate of benefit accrual, the employer chose not to inform participants about these effects so they could, the Amara v. Cigna Corp. court claimed, ease the transition to a retirement plan that was less favorable than the previous defined benefit plan. CIGNA even explicitly instructed the consulting company that helped them produce the 1997 Newsletter and 1998 Retirement Kit, “not to compare the old to the new plans” in those two documents. A very similar request was made by the employer to their actuaries. CIGNA’s assistant vice-president of global benefits wrote in an internal email that “[w]e continue to focus on NOT providing employees before and after samples of the Pension Plan changes” and when one of the benefits counselors was requested to provide these comparisons the counselor replied “we don’t do that”. The plan administration at the time of the 2008 trial confirmed that “as a general rule the policy was that employees would not be provided with comparisons between
their benefits under the old plan and the new plan.” CIGNA’s presidents were responsible for the substantial shift of focus on positive aspects of the cash balance plan in their plan disclosures and they understood the risk of an adverse employee reaction if the true severity of reductions in the rate of future benefit accrual were known—in September 1998 several articles appeared on cash balance conversions at other companies and in some cases the complaints of employees resulted in a partial or complete rollback on their cash balance amendments. CIGNA avoided a similar revolt within their company—it was reported to the board of directors that “CIGNA’s Cash Balance plan has been very well received by CIGNA employees (employee survey ratings up 15 percentage points) and has not generated notable controversy”. The court concluded that CIGNA was aware of the significant rate of future benefit accrual, that it would affect a substantial proportion of its employees, and that it wished to avoid and negate adverse reactions from employees. This was the reason its §204(h) notice was not in compliance with ERISA. The court also found that the SMM and SPDs failed to disclose the possibility of wear-away. CIGNA admitted that it did not inform employees that they may not be accruing benefits under the cash balance plan but argued that disclosure on this wear-away concept was unnecessary. Their reasons for this claim are that the wear-away was an unpredictable “idiosyncratic contingency”, that the wear away was as a result of an accumulation of plan provisions as well as unpredictable circumstances such as the interest-credit Treasury bill index, and that the wear away only had the potential of affecting a small number of participants (Amara v. Cigna Corp., 2008). A second circuit judge had earlier ruled that an ERISA fiduciary was not required to be “perfectly prescient as to all future changes in employee benefits” but also that “when a plan administrator speaks, it must speak truthfully” (Mullins v. Pfizer, Inc., 1994). In Becker v. Eastman Kodak,
another second circuit judge claimed that “an SPD need not anticipate every possible idiosyncratic contingency that might affect a particular participant’s or beneficiary’s status”. This same judge took a narrow view of what constituted an “idiosyncratic contingency”—the judge equated it to the sudden death of the participant (Becker v. Eastman Kodak Co., 1997). The Amara v. Cigna Corp. court motioned that wear-away was a relevant structural phenomenon and that CIGNA predicted it despite the interactions of numerous plan provisions and falling interest rates. The rate at which opening account balances were determined, the use of a mortality discount, and the exclusion of early retirement benefits practically guaranteed that wear-away would occur if interest rates had fallen. Though CIGNA claimed that the rapid decline in interest rates following the implementation of the cash balance plan was entirely unexpected, interest rates had already fallen by 1% between 1997 and 1998—when CIGNA published the first part of the cash balance plan SPD. For this reason, the court found that CIGNA had a duty to alert participants of the possibility of wear-away in its disclosures regarding the cash balance plan.

The fact that CIGNA created a Qualified Plan that was structurally susceptible to wear-away alone created the responsibility to produce disclosures on wear-away. Also, the court disagreed with CIGNA’s claim that wear-away only had the potential of affecting a small number of participants because it understood that wear-away had a dramatic effect on even just the plaintiffs alone—some had no benefit accrual from the implementation of the cash balance plan all the way up to their retirement. The court found that CIGNA’s disclosures were not only insufficient but also misleading. The 1997 Newsletter stated that after establishing an opening account balance that the participant “will begin earning retirement benefits”. Its 1998 SPD stated that the individual participant account and credit system would grant the participant the “ability
to earn retirement benefits throughout [the participants’] career”. In another portion of the SPD it states that “[u]nder the plan, your benefit will grow steadily throughout your career as credits are added to your account”. To this conclusion, CIGNA argued that “the fact that the SPD told Plan participants that they might receive their protected Minimum Benefit if it was higher than their cash balance benefit was a clear indication that a participant’s prior protected benefit might be greater than his or her account balance, and that there might be a period of time during which there would be no increase in his or her overall pension benefit”. The court disagreed with CIGNA’s contention that the participants received the required degree of notice concerning wear-away because nowhere else in the notices is wear-away, or any equivalent phenomena, given any further discussion. Given the fact that the aforementioned statements in CIGNA’s disclosures unequivocally state that all participants will begin accruing benefits under the cash balance plan starting January 1, 1998, the court found that participants would reasonably believe that wear away was not an element of the cash balance plan—there was no statement in the notices that informed any participants of the possibility that they were not earning retirement benefits. This indirect reference to wear-away was inadequate (Amara v. Cigna Corp., 2008).

Early Retirement Benefits; Annuity & Lump Sum Distributions

Another argument by the plaintiff against CIGNA’s disclosures was that they led participants to believe that their accrued benefits under the cash balance plan were protected, particularly early retirement benefits. The disclosure stated that if former participants under the defined benefit plan chose an annuity distribution under the cash balance plan then they would receive all of their early retirement benefits. However, the early retirement benefits were
excluded from the lump sum distribution because they were excluded from the calculation of opening account balances. CIGNA’s disclosures gave participants the reasonable impression that their early retirement benefits were fully protected as part of either their minimum benefit or their initial account balance under the cash balance plan. The November 1997 newsletter stated that “[i]f you earned a benefit under the current Pension Plan, the lump sum value of that benefit as of December 31, 1997 will be transferred to your account as your opening balance” and the December 1997 Retirement Kit stated that “[a]ny benefits that you have earned under the Pension Plan through December 31, 1997, are fully protected and their value will be reflected in your new plan balance”. Other statements to this effect were given in other disclosures. The court found that these notices were not written in a manner calculated to be understood by the average plan participant not only because participants could reasonably conclude that their early retirement benefits were protected when they were not but also because participants were given the impression that all of their benefits were being protected regardless whether they chose an annuity or a lump sum. It was not until July 2006 that CIGNA informed participants, in a coherent manner, that there were restrictions on the availability of early retirement benefits if the participant chose a lump sum distribution (Amara v. Cigna Corp., 2008).

Plaintiffs claimed that CIGNA failed to comply with regulations requiring them to provide participants with information regarding the relative values of different benefit forms available to them upon retirement. They asserted that CIGNA was required to and did not inform plan participants:

1. That the lump sum option did not include early retirement benefits available as part of the annuity.
2. That the annuity option was more valuable than the lump sum option.

3. There was a disparity between the defined benefit plan and cash balance plan benefits; the comparisons between the values of the two benefits.

4. Whether waiting for a future date to receive benefits would result in a higher amount of benefits.

They argue that without this necessary information some participants chose a lump sum distribution when an annuity would have been more valuable (Amara v. Cigna Corp.).

The terms of the cash balance plan stated that upon retirement a participant with accrued benefits under the defined benefit plan may choose upon retirement between either their cash balance plan benefit as a lump sum or their defined benefit plan benefit as an annuity. The lump sum could not be less than the equivalent actuarial value of the participant’s minimum benefit; however, this minimum benefit did not include early retirement benefits (with the exception of the preserved spouse’s benefit). On the other hand, the annuity included all early retirement benefits that the participant was eligible for under their defined benefit plan. The plaintiffs relied upon ERISA sections 203(e) and 205(g) which both required the written consent of a plan participant before retirement benefits exceeding $5,000 can be distributed as a lump sum. Treasury Regulation 1.401(a)-20, Q&A-36 stated that starting plan years beginning after December 31, 1988 participants must receive a general description of material features concerning optional forms of benefit as well as material that explains the relative value of these optional forms. Under the Code of Federal Regulations § 1.417(e)-1(b)(2)(i) a lump sum distribution is not valid if the participant does not receive a disclosure that satisfies the requirements of the aforementioned treasury regulation. For these reasons the court agreed with
the plaintiffs that CIGNA had a legal obligation to notify participants that the early retirement benefits under the defined benefit plan were only available through the annuity distribution option. It claimed that including early retirement benefits in the value of the annuity distribution without making clear that these benefits were not available under the lump sum option constituted insufficient disclosure. The court found that CIGNA violated ERISA and relevant Treasury regulations because they treated these two forms of benefits on their disclosure as though they were substantially equal; they should have included an explicit statement that early retirement benefits accrued under the old defined benefit plan were only available under the annuity form of distribution and were not part of the lump sum payment (Amara v. CIGNA Corp., 2008).

The court disagreed with the plaintiff’s assertion that they were not in compliance with applicable law when they had not informed participants that the annuity option was more valuable than the lump-sum option. More recent regulations issued on October 2004 identify this problem and address a solution stating that “the description of the relative value of an optional form of benefit compared to the value of the [annuity] must be expressed in a manner that provides a meaningful comparison of the relative economic values of the two forms of benefit without the participant having to make calculations using interest or morality assumption”. The court assumed that because this explicit treasury regulation was issued in 2004 this meant the previous version of the treasury regulations on the subject of annuity/lump sum value disclosure had not resolved to address this matter with this particular solution. They ruled that although employers could have chosen to provide present value comparisons between the lump sum and annuity options previously, they were not required to do so before the new 2004 regulations went
into effect. CIGNA expressed to the court that it had adjusted its disclosures to become in compliance with the new regulations after their effective date—it offered any employee that chose a less valuable benefit an opportunity to reconsider their choice. CIGNA’s expert testified that if they had disclosed the present value of the annuity as well as the lump sum without further information they may have been misleading the participant. He also testified that not presenting a present value comparison was standard practice within the industry. The court held that even though the present value of the annuity may exceed a lump sum there was no unilateral disadvantage of one option over the other because the employee receiving the lump sum may benefit from the opportunity to invest the lump sum at their own discretion (Amara v. Cigna Corp., 2008).

Concerning the plaintiff’s claim that CIGNA had wrongfully neglected to inform participants with comparisons of ancillary benefits between the defined benefit plan and cash balance plan as well as failed to inform them on whether waiting for a future date to receive benefits would result in a higher amount of benefits, the court found that even though there is no support in the regulations that CIGNA was obligated to make these disclosures they still assumed an obligation because of statements they made in their disclosures. For example, CIGNA wrote in their 1998 and 1999 SPDs that “[y]our final Plan benefits cannot be less than your old plan benefits on December 31, 1997. If this minimum benefits rule applies to you, you’ll be notified by the Retirement Service Center when you request a distribution”. The plan administrator at the time of the trial admitted that there was no specific disclosure that informed participants that they were going to be distributed the minimum benefit but instead CIGNA offered participants an 800 number to call to ask specific questions about the calculation of benefits. The court disagreed
with CIGNA’s argument that simply including the annuity under the defined benefit plan as a
distribution option was enough to inform them that the minimum benefits rule applied to them.
However, the court found that CIGNA was under no obligation to inform participants that they
would eventually qualify for retirement benefits under their defined benefit plan if they
postponed retirement. An example of this concept was that one of the Class members elected a
lump sum distribution at age 54—had he waited until age 55 to retire he would have become
eligible for early retirement benefits that would have granted him an annuity with twice the
present value of the lump sum he received. Plaintiffs argued that this participant should have
been informed of this prior. CIGNA argued that the treasury regulations on this matter only
require them to inform participants on the benefits for which they are eligible and this participant
was not eligible for that particular benefit yet. The court agreed with CIGNA and stated that to
require otherwise would present a heavy administrative burden and no clear stopping point for
obligations on the employer’s disclosure (Amara v. CIGNA, 2008).

j. Was There Injury?

CIGNA’s primary argument in response to the plaintiff’s inadequate disclosure claims
was that even if they were defective the plaintiffs were entitled to relief because they could not
demonstrate any injury done as a result of these inadequate disclosures (Amara v. Cigna Corp.,
2008). In Frommert v. Conkright, a case with a similar 204(h) contention, the judge emphasized
the broad nature of ‘likely harm’ because he ruled that the “[plaintiffs] were deprived of the
opportunity to take timely action in response to the purported ‘amendment’. Such action might
have included seeking injunctive relief, altering their retirement investment strategies, or perhaps
considering other employment”. The judge also stated that “[i]mposing a requirement that plan participants must show actual prejudice from a challenged plan amendment by terminating their employment imposes an unduly harsh burden on dissatisfied plan participants” (Frommert v. Conkrignt, 2006). CIGNA asserted that there was no injury because (1) “none of the named plaintiffs left CIGNA as a result of perceived deficiencies in [the cash balance plan] or the related notices and disclosures”, (2) the plaintiffs received sufficient information on their new cash balance plan from sources—including their opening account statements and total compensation reports—that cured any defects in any disclosures required by ERISA, and (3) even if the named plaintiffs received the information they claim was required and missing from disclosures their benefits under the cash balance plan would not have changed. The court did not consider the additional materials provided by CIGNA sufficient to cure the disclosure defects or “transform any possible [injury] into harmless error” (Amara v. Cigna Corp., 2008).

The court rejected CIGNA’s argument that no injury occurred to the plaintiff’s class because none left employment on the grounds that the absence of certain required disclosures and the inclusion of inaccuracies in publications relating to the plan were likely to have led participants to believe that all the undesirable components of the amendments converting their defined benefit plan to a cash balance plan were not components within the amendment and new plan. The court also rejected CIGNA’s third argument—no injury was made because the participant’s benefits would not have changed had they received the degree of disclosure they claim they should have received—on the grounds that previous courts rejected the notion that the plaintiff could not have received injury if there was nothing they could have done to change their benefits in the first place. Ms. Amara herself testified that, had she been informed at her rehire
interview that she would be undergoing a wear-away period wherein there would be no additional retirement benefit accrual she could have “negotiated for a higher salary”, “looked and talked to other employers”, or stayed at her previous position (Amara v. Cigna Corp., 2008).

k. The Court’s Remedy for CIGNA’s Inadequate and Misleading Disclosure

The US District Court of Connecticut believed that the remedy for CIGNA’s disclosure misrepresentations would be to adapt the execution of the plan effective January 1998 to reflect how it was represented in the Summary Plan Description. Because CIGNA disclosed to its employers that their benefit will “grow steadily throughout your career” this means that the SPD created a reasonable expectation to participants that the cash balance plan would protect all prior defined benefit plan benefits. Because the case was brought about under ERISA §501(a)(1)(B)—to recover benefits due—the court decided to implement benefit accrual to the plaintiff’s class under the plan to equal the accrued benefit under their defined benefit plan plus the accrued benefit under the cash balance plan—the A + B method. This approach contrasts with CIGNA’s approach to provide the greater of defined benefit or cash balance—the A or B method. The remedy was called for because the participant’s recovery needed to be based upon the sort of plan the participants thought they were going to receive given the SPDs and other notices. The disclosures did not mention wear-away, this approach removes wear-away. There was no mention in the disclosures of the potential for a loss in early retirement benefits under certain circumstances, now they will always have these benefits. The controversial determination of an opening account balance without early retirement benefits will become immaterial because the participant’s opening balance will be zero and any additions will be credits added to their defined
benefit plan accrual. Adding together both plan benefits also remedies CIGNA’s failure to notify employees that early retirement benefits were only available under the defined benefit plan annuity distribution because all prior defined benefit plan benefits would be automatically be provided in an annuity form. This approach also cures their failure to provide participants with a notification that the minimum benefits rule applies to them. The court found that—given their limited authority—there were no concrete means of remedying the impression that the summary of material modification made to participants that cash balance plan benefits were roughly comparable to those of the defined benefit plan. (Janice C. Amara v. Cigna Corp., 2008).

II. Employer X, LLC

a. 204(h) Notice & Previous DB Plan Benefits

On June 2008 Employer X, LLC adopted an amendment converting its defined benefit plan to a cash balance plan effective January 1, 2008. The plan name was changed from Employer X, LLC Defined Benefit Plan to Employer X, LLC Cash Balance Plan. The plan document was individually drafted by Employer X’s attorney which means they are required to amend and restate the plan for the Economic Growth and Tax Relief Reconciliation Act of 2001 (“EGTRRA”) as well as other current legislation sometime between February 2009 and the end of January 2010. They must then submit the plan to the Internal Revenue Service for approval and receive a favorable determination letter (see exhibit 1 in Appendix A for pg. 2 of attorney’s letter dated May 23, 2008).

The attorney provided them with a §204(h) notice (see exhibit 2 in Appendix A for pg. 1 of the 204(h) notice). This notice included the statement, “In no event will your benefit be less
than the benefit you have earned under the [defined benefit plan]” and that “the benefit you earn under the new formula could be more or less than the benefit you would have earned under the plan had it not been amended”. This is a clear disclosure of the likelihood that benefits may be reduced for the participant, this often happens as a result of the conversion from a defined benefit to a cash balance plan. As mentioned earlier, this is almost unilaterally the case unless the cash balance plan is remarkably generous to the participant because the defined benefit plan normally includes a final or a final-average index to derive benefits whereas the cash balance plan accumulates a final benefit that is indirectly indexed against career average earnings. In Atlantic Advisor’s case this conversion clearly has a similar impact upon participants’ final benefits. The §204(h) notice goes on to describe the old benefit formula, in compliance with post-2001 requirements that the notice describe the benefit allocation prior to the amendment’s effective date as well as the benefit allocation after the amendment’s effective date. It stated that until June 2008 the defined benefit plan formula was “traditional” and benefits were defined based upon highest average pay and years of service. The formula was 10% of the average compensation over the 3 years of the participant’s highest pay times years of credited service not to exceed 10 years. This defined benefit formula was extremely generous because it granted the participant very large growth over a ten year period and a total of 100% of highest average compensation after only ten years of service. The notice goes on to state that participant’s benefits under their previous plan will be frozen as of June 2008—the years of credited service and new average compensation are no longer factored into the participant’s final benefit with respect to the old formula. This means that not only were participants no longer allowed to receive an extra ten percent of their greatest average pay per year, it also means the percentage of benefit they
receive will not be based upon their career earnings, just pre-June 2008 earnings. Average-
highest or final-highest earnings have historically been a remedy to concerns that retirement
benefits will not remain abreast of rising inflation, cost or living, and even the participant’s
standard of living. The notice then states (see exhibit 3 in Appendix A for pg. 2 of the 204(h)
notice) that the new pension formula will take effect on the same day that the old defined benefit
plan assets were frozen. It also states that the new plan benefit will be added to the frozen benefit
in order to determine the total benefit under the plan. This disclosure illustrates that the new plan
is drafted in compliance with the Pension Protection Act of 2006 (“PPA”) which added ERISA
§204(h)(5)(B)(ii) stating that participants subject to a defined benefit plan conversion cannot
have a benefit less than the sum of their accrued benefits for years of service prior to the
effective date of the amendment and accrued benefits for years of service after the effective date
of the amendment.

b. Initial Account Balance?

The disclosure also states that their new benefit will be the value of their cash balance
account determined by contribution credits that are a percentage of total compensation and
interest credits for each year until distribution. Additionally, all participants’ initial cash balance
account will be zero. This detail is in contrast to CIGNA’s method of calculating an initial
account balance based on a present value of the future defined benefit annuity due. As previously
mentioned, there are no regulations requiring a particular method of determining the participants’
initial account balance upon conversion from a defined benefit plan to a cash balance plan—the
very concept and approach is entirely at the discretion of the employer. So why did CIGNA
calculate an initial account for each participant when they could have just given zero treatment to previously accrued benefits after establishing a minimum benefits rule? The approach CIGNA took greatly reduced wear-away for all participants—they would otherwise have had to re-earn all of their minimum benefits before being able to grow their benefit accrual. This approach may also have, arguably, been a further attempt by CIGNA to conceal the significant reduction in future potential benefit accrual by granting non-grandfathered participants an account balance with a value which they can witness rise overtime through their annual account statements. Their other attempts to lighten the participants’ perception concerning the grave reduction of benefits resulting from the cash balance amendment through defective plan disclosures would suggest that their motives were to limit transparency by actively limiting doubt on the part of the participants. Employer X’s need to comply with the regulatory requirements that they provide a benefit equal to prior accrued benefits plus a benefit accrual after the amendment renders the concept of calculating an initial account balance to be somewhat functionally redundant with the exception of interest credit accruals. If they were to calculate an initial account balance then they could exclude the initial corpus in order to ensure that additional accruals based upon compounding interest would be the only factor to raise their future benefit and would ultimately be included among benefits earned after the defined benefit conversion amendment. When considering the benefit accrual already earned, this would have been a great way to gradually increase the participant’s benefit for the purpose of keeping the participant’s benefit abreast of increases in living costs and inflation particularly if the interest credit is indexed against the interest rates on U.S. Treasury bills. This is another instance where benefit accruals that have been historically utilized for the purpose of adjusting a participant’s benefit for inflation and cost
of living are removed by plan amendments implemented for the purpose of converting a defined benefit plan to a cash balance plan. Granted, if Employer X had implemented interest credit accrual the way CIGNA had—the return on 5-year treasury bills plus .25% not to exceed 9% or be lower than 4.5%—they would be receiving a more generous benefit than a cost of living adjustment would require. However, this would still not be taking into account rising compensation, which was frozen, it would only be taking into account average compensation par the structure of the cash balance plan accrual. In fact, assuming the same 4.5% annual salary increase used in the Amara v. Cigna Corp. example illustrating that the defined benefit plan accrual rate was approximately twice the cash balance plan accrual rate relative to final pay, the interest accrual would only reflect average salary increases because treasury bills are not likely to rise past 4.5%. Thus, this alternate approach could either be considered a supplement for future salary increases or insurance against inflation and the rising cost of living. In either case, this approach was not implemented by Employer X which illustrates the loss of the structural safeguards inherent in the participant’s previous method of benefit accrual. These disadvantages persist despite the protections under ERISA §204(h)(5)(B)(ii).

c. Definition of “Compensation”

The notice goes on to state that beginning January 2008 credits would be contributed to the participant’s account at the end of each plan year based upon their total compensation. Their compensation is defined in the notice as “wages, salary, fees for professional services and other amounts received for personal services rendered in the course of employment”. In section 5 of the Adoption Agreement (“AA”) compensation for the purpose of the plan is defined as “Code
§415 Compensation” with “no exclusions” (see exhibit 5 in Appendix A for pg. 4 of the Adoption Agreement). ERISA §415(c)(3) defines “participant’s compensation” simply to mean “compensation of the participant from the employer for the year”. With no exclusions chosen, Employer X had forgone the option to credit participant’s accounts a smaller amount than they would have otherwise. For example, if bonuses were excluded then an employee that makes more than half of their total salary in bonuses would be credited a much smaller percentage of their total compensation than somebody that makes all of their salary in non-bonus compensation. This could create plan qualification issues if these practices result in a Qualified Plan that is discriminatory against certain employees. The notice also states that the participant’s total compensation may be limited to the legal maximum established by the IRS which was $230,000 for the calendar year in which the amendment was effective. This legal maximum is established by ERISA §415 and §401(a)(17) which states that a “trust shall not constitute a qualified trust under this section unless…the annual compensation of each employee taken into account under the plan for any year does not exceed $200,000” which is increased by $5,000 for cost-of-living adjustments. This limitation proportionally lowers the utility value of a Qualified Plan to any participant that receives compensation exceeding this amount. This particular limitation applies to nondiscrimination, defined benefit plans, and defined contribution plans but the nature of the cash balance individual account format allows for heavy applicability to the annual compensation limit because the employer’s contribution credit is a fixed percentage of the participant’s annual salary.

The 204(h) notice goes on (See exhibit 4 in Appendix A for pg. 3 of the 204(h) notice) to describe the interest credits applied to the participant’s account, “[t]he interest crediting rate is
determined each year and is equal to the interest rate published”. This illustrates the permissibility of selective ambiguities within the 204(h) notice—while the notice specifically illustrated the formula determining the participant’s benefit under their prior defined benefit plan it defined no particular percentage of compensation for their annual credit and no interest rate to compound their annual credit. However, Treasury Regulations 54.4980F-1 Q&A-11 asserts that if the amendment reduces the rate of future benefit accrual then the 204(h) notice “must include a description of the benefit allocation formula prior to the amendment [and] a description of the benefit or allocation formula under the plan as amended”. This notice, alone, clearly lacks the description of the cash balance plan required by this regulation. It is possible that given the required A+B benefit accrual approach taken by Employer X that there was no future reduction in future benefits. This is somewhat likely given the fact that the company is a closely held LLC with a plan that accrues nearly full benefits after only 10 years of service. However, the first effective date of Employer X’s defined benefit plan was January 1, 2004 (see exhibit 6 in Appendix A for pg. 2 of the DB plan document)— the first participants only made accruals based on at most 4 years of service. The participants’ accrual, even if carried over without wear-away, was theoretically reduced given the career average nature of the cash balance plan as well as the reduced annual benefit credit that resulted.

d. Are They Obligated to Provide a 204(h) Notice?

A Comparison of Participants’ Benefit Accrual; Review of the Census

Section 5 in the Adoption Agreement of Employer X’s cash balance plan (see exhibit 5 in Appendix A for pg. 4, 5 and addendum 1 of the AA) partitioned all employees into groups and
defined the annual contribution credits made to each group. Group A is the owner and managing member of Employer X and he received a contribution credit “equal to 100% of the Maximum Contribution Credit”. This Contribution Credit is defined in the Plan Document (see exhibit 7 in Appendix A for pg. 15 of the Plan Document) as “equal to 10% of the actuarial present value of the Defined Benefit Dollar Limitation applicable to the Participant for the Plan Year”. This references 26 U.S.C. §415 which states that a trust is no longer a qualified trust—no longer receives benefits due to Qualified Plans under ERISA and is, thus, disqualified—if “[annual] benefits with respect to a participant exceed…the lesser of $160,000 or 100 percent of the participant’s average compensation for his high 3 years”. This annual benefit would be in the form of a straight life annuity and the $160,000 is adjusted annually by a multiple of $5,000 at the discretion of the Secretary of the Treasury. The defined benefit limit as of 2008 was $185,000 which means that—given the plan language “for the Plan Year”—the present value of a straight life annuity that would have provided an annual benefit of 18,500 after retirement was added to his account balance at the end of the 2008 plan year. This means that he receives approximately one tenth of his maximum benefit every year. Given that his compensation has been far greater than the §401(a)(17) annual compensation limitation (see exhibit 8 in Appendix A for the employee census) and that every participant received an extra ten percent of their compensation every year under the old defined benefit formula, it is not likely that the owner/managing partner experienced any reduction in future benefit accrual. The rest of the employees are granted a more typical credit allocation—the owner’s spouse (Group B) receives 40% of compensation annually, the “Trading Principal” (Group C): 30%, the “Business Development Principal” (Group D): 30%, the Director of Marketing (Group E): 10%, the spouse
of “Trading Principal” (Group F): 50%, the Senior Vice President of Trading (Group G): 0%, and all other Employees (Group H): 7%. (I will not be discussing the non-discrimination issues surrounding these disparities due to the appalling degree of explanation necessary including a thorough examination of Employer X’s supplemental 401(k)). The plan only credited the participants’ years of service (see exhibit 9 in Appendix A for page 8 of the DB plan adoption agreement) so the sole member of Group H that became a participant on July 1st, 2007 had not yet accrued any vested or un-vested benefit. Group H accumulated service based upon years after becoming a participant because the plan was amended before her hire to begin crediting only service as a participant. Before this, when Groups A, B and D were the only other employees at Employer X, the plan credited service based upon total service since hire not counting breaks in service. This amendment was beneficial to these initial three participants because they created an extra free year wherein they were not required to fund this particular participant’s accrual. Given the particularly generous nature of the Employer X’s defined benefit plan the savings were large. If Group H had accumulated one year of service the participant would have accrued an annual benefit of approximately 4,266 (42,655*10%  see exhibit 10 in Appendix A) payable upon retirement. The present value of this based on certain annuity assumptions would be the additional funding liability for the Employer. This amendment to credited service was nondiscriminatory and did not apply to the other groups because it was enacted before Group H’s hire. The only employees that had accrued a benefit were Group A, B, and D. Group B was fully vested in the accrued benefit, had 5 years of credited service at 2008 and thus accumulated an accrual of 50% highest average compensation earned before 2008. This participant’s new benefit would be a contribution credit of 40% of compensation annually. This would be compounded by
an interest credit rate equal to 30-year Treasury securities (see exhibit 5 in Appendix A). This information confirms that there was a general reduction in future benefit accrual on at least one participant—the old accrual and highest average service calculation was frozen and the new benefit provides only a career average benefit based upon only 40% of the participant’s compensation, less than the percentage the participant earned at the time of the amendment. It is noteworthy that the 204(h) notice was entirely clear on disclosing the fact that the old benefit will be reduced. Also, unlike CIGNA the notice makes no assertions with respect to the benefits of this amendment. Whereas CIGNA’s notices make claims about benefit “enhancements” et cetera, Employer X’s 204(h) notice simply states that “depending on your circumstances, the benefit you earned under the new formula could be more or less than the benefit you would have earned under the plan had it not been amended”. Group D was under similar circumstances only they had accrued benefit equal to 30% of her compensation upon the defined benefit plan conversion and was subsequently entitled to a contribution credit of 30% of her salary. As previously discussed, the compounding interest credit could reasonably be considered a supplement to future salary growth. Thus, it is theoretically possible that she receives an equal or greater benefit accrual than she had under the cash balance plan especially if Group D’s salary never rises over time. This notice, though not materially in compliance with regulations, is nonetheless very truthful in its assertions—some participant may earn more, some may earn less “depending on your circumstances”.

To supplement this point, there is no regulatory imperative for an employer to investigate the impact a defined benefit plan amendment has on its participants’ future benefit accrual. Therefore, the employer is under no obligation to engage in the preliminary activities that would
determine whether 204(h) notices are necessary. Any penalties for deficiencies on the contingency requirement concerning the 204(h) notice would have to arise from litigation and from there it would have to be proven that the employer was aware of material reductions in participants’ future benefit accrual. Granted, it could be argued that Employer X had already indicated that they were aware of material future benefit accrual reductions because they issued a 204(h) notice in the first place; perhaps disbursing a 204(h) notice without foreknowledge of future benefit reduction reflects precautionary practices. This precaution, however, still lacks the necessary description of the plan as amended. Also, given the fact that participant disclosures will not be reviewed by either the DOL or the IRS except in the instance of an audit or other investigation, there are few immediate penalties for vague content within a 204(h) notice. This means that any employer that lacks any reason to believe an investigation will occur would not have very much incentive to be in compliance with the many disclosure regulations established by the IRS and the DOL. Very large employers are typically audited every year and small employers such as Employer X are a lot less likely to be targeted for an audit. On a relative scale, this means that the need for disclosure becomes more a matter of providing greater transparency to the employees in order to preempt any backlash or complaints they may have to the DOL if any changes were not made apparent.

_Interest Credit on the 204(h) notice_

Employer X’s 204(h) notice simply stated that interest credits “are determined by multiplying your account balance on January 1 by the interest crediting rate for the plan year” and that the interest credit will be prorated for the year in the event that the participant terminates
employment. This means that the fraction of the year passed before termination would determine the fraction of the entire interest credit that would otherwise have been granted. This degree of clarity is conducive to an effective 204(h) notice except it omits the fact that the interest credit rate is indexed based upon 30-year Treasury securities. This omission is likely immaterial because the interest credit is not particular to any class of employee and the notice does not indicate otherwise in its statements. The notice’s silence on specifics does not prevent the participant from asking the plan administrator—the notice concludes with the statement, “If you have any questions, please do not hesitate to contract me”.

The 204(h) Notice: “Comparing Old and New Formulas”

Finally, under the last heading in the Employer X 204(h) notice titled “Comparing Old and New Formulas” (see exhibit 4 in Appendix A) the disclosure states:

In some cases, the new pension formula will provide a better pension benefit than would have been provided under the old formula. There may, however, be instances where the old formula would have provided a better benefit had it continued to apply.

Treasury Regulations 54.4980F-1 Q&A-11 asserts that if the amendment reduces the rate of future benefit accrual then the 204(h) notice “must include sufficient information for each applicable individual to determine the approximate magnitude of the expected reduction” and that “any case in which it is not reasonable to expect that the approximate magnitude of the reduction…will be apparent from the description of the amendment…further information is required” and that this information is sufficient if it includes “one or more illustrative examples showing the approximate magnitude of the reduction” for the individual receiving the notice. It
also states that examples are required for any change in a defined benefit plan that involves wear away. Because Employer X’s amendment is an A+B conversion from a DB to a Cash Balance there is no wear-away. The language of the regulation indicates that examples are generally sufficient but not necessary to illustrate the magnitude of reduction, they are only necessary in the case of wear-away. This is another instance where Employer X’s 204(h) notice is missing information that regulations require. Granted, the contingency is based upon whether the new plan reduces future benefit rate accrual and the 204(h) notice states that the participant may or may not have a future benefit accrual reduction. Having observed the Participant’s prior and subsequent benefits this has been deemed to be the case.
CHAPTER III: CONCLUSION

These two cases highlight the concept that the degree of ownership concerning a Qualified Plan is contingent upon the activities undertaken by the Employer with respect to the plan. Most notably, ownership of the Qualified Plan is only entirely granted to the Employer under two particular circumstances. These circumstances are (1) the IRS and DOL do not determine that the Plan is contrary to ERISA in form or execution and (2) the courts do not deem that the Plan Sponsor (Employer) has inflicted injury upon any participants. This latter point is demonstrated by the 2008 Amara v. Cigna Corp court’s decision to modify the form and execution of CIGNA’s plan retroactively. They ruled that CIGNA Corp. must adapt the execution of their plan effective January 1998 to ensure that their conversion followed the “A plus B” method of DB-to-cash balance conversion instead of CIGNA’s choice of the “A or B” method. The Pensions Protection Act of 2006 added section §204(h)(5)(B)(ii) to ERISA which established a new requirement for all employers implementing a cash balance plan to take an A+B approach for all DB to cash balance plan transitions after June 29, 2005. This means that the participant’s cash balance plan credits must represent accrued benefits that are added to the already accrued DB plan benefits. This means that CIGNA’s inadequate disclosure to participants simply resulted in the employer missing the opportunity to implement an “A-or-B” approach—the greater of accrued cash balance plan benefits OR accrued defined benefit plan benefits (Janice C. Amara v. Cigna Corp., 2008). Congress had already been called upon by pension experts as early as 2000 to pass legislation guaranteeing that the DB plan accruals are guaranteed to the participant before additional accruals under the cash balance are added as a
supplement to their already earned benefit (United States Congress, 2000). CIGNA’s forced conversion to an A plus B method in their DB plan conversion up to 2008 also means that CIGNA was forced to cede their ownership of the plan by the Second District Court of Appeals.

The reversibility of amendments and resultant accruals within a plan indicates a lack of ownership by the employer. It is noteworthy that CIGNA’s revocation of ownership only applied during the time period between the effective date of the amendment and the court’s ruling on the impermissibility of the amendment. The Employer upon compliance will thereafter have complete control over the Qualified Plan again and can pass any amendment they wish. To reiterate, there is no requirement that a plan qualified under ERISA may not have participants experience wear-away. Therefore, CIGNA is certainly permitted to pass another amendment reducing future potential benefit accruals but the court’s mandate ensures that all participants accrue their benefit first—the benefit that is not permitted to be reduced under the anti-cutback rule. CIGNA’s 1998 conversion amendment was not impermissible for its inherent illegality per se but was impermissible given the Employer’s attempts to conceal the amendment’s effects upon the participant. They also treated the lump-sum distribution as equal to the annuity distribution even though the lump-sum excluded the participant’s accruals in early retirement benefits. Since the SMM, the SPD, and the 204(h) notice gave the impression that benefits would always grow CIGNA is now forced to change its formula to ensure that this is true despite never having signed an Adoption Agreement or executed a Plan Document to this effect. The mandate was to establish the sort of benefit the participant would presumably have expected to receive given the language of the disclosures they received by CIGNA (the lump-sum and annuity disparity becoming void because the DB benefits including early retirement benefits would be
distributed as an annuity no matter what the participant did with the cash balance portion of their distribution). The act of compliance to this mandate will be a government action and not an act based upon the Employer’s ownership of the plan.

Not all insufficient disclosures required remedial action as a result. Even though participants may be injured by CIGNA’s silence on the fact that the annuity option provided more benefits than the lump-sum distribution, applicable law and regulations had not mandated them to do so and therefore it was permissible. It was not until October 2004 that regulations to this effect were published and at that point CIGNA began to provide sufficient information to participants on this matter. What had been standard practice in the industry and was not in contradiction with published regulations was permissible—this alone did not result in a cessation of plan ownership for the plan years up to 2008. What did result—along with the rest of their transgressions—in the cessation of the plan to the federal government were CIGNA’s misleading statements to the participants that gave the impression that the lump-sum option was equivalent to the annuity option. Similar to material omissions in required disclosures to participants, being found by a court to have misled the participant directly resulted in a cessation of ownership to the federal government. This type of misleading statement included CIGNA’s claim that they would notify the participant if the minimum benefit rule applied to them because they had not done so.

CIGNA attempted to argue that there was no injury because participants could not prove that they would have performed any significant action if all the inadequate and misleading disclosures were portrayed appropriately. The court established that injury could be made to the participant when the Employer intentionally removes their opportunity to make timely action in
response to any amendments to the plan. This illustrates ERISA’s legislative intent with respect to the SMM, SPD, and the 204(h) notice. Because the IRS and the DOL do not review disclosures except in the case of an audit or other investigation, scrutiny by the courts has generally been the primary means by which Employers could be forced to cede ownership of the plan due to the inadequacy and/or inaccuracies of their disclosures. For this reason participants must often be wary of their Employer because there is little authoritative oversight over the content of their disclosures.

The Amara v. Cigna Corp. case illustrates that the Employer must cede ownership of the plan during the years the courts deem that an injury has been dealt to participants. The Employer X, LLC study conversely reveals that there happens to be a lot more comprehensive plan ownership when the Plan Sponsor is a small closely-held business. The case brought against CIGNA was a class action lawsuit involving tens of thousands of current and former participants against their Employer. This class action approach made it a lot easier to pool resources in order to attempt to retrieve the benefits to which they thought they were entitled. This particular approach would be nearly impossible for a participant in a plan sponsored by a small Employer. This is one of the key reasons that the small Employer has less concern for strict compliance to ERISA relative to large employers. While all individually drafted plans—the kind that would be preferable for Employers wishing to maximize influential HCEs’ benefit—need to be submitted to the IRS for a favorable determination letter, the disclosures to participants in particular are not under scrutiny by the IRS. Also, the IRS generally audits large Employers every year whereas small Employers are audited at random. Thus, small employers are under significantly less risk of being forced to cede ownership of their plan to the government.
Employer X’s 204(h) notice did not adequately compare their old DB plan accrual to the cash balance plan accrual. Their noncompliance with Treasury Regulations were not nearly as demonstrative of deceit as they were in the CIGNA case but it is still noteworthy how little disclosure is permissible given the lax regulations and oversight over them. Because no complaints were filed and no resultant investigation was made, this sort of disclosure passed its very informal compliance test without adhering to certain regulations specific to the 204(h) notice. It is clear that the Employer was obligated to provide participants with a 204(h) notice because Group B’s future benefit accrual was obviously reduced and it is very likely that all of the other Employees’ potential benefit accruals—with the exception of the owner—were reduced as well. Because there is no regulatory imperative for an employer to investigate the impact of a DB to cash balance amendment, vague language with respect to comparisons appear to be appropriate for the purposes of 204(h) notice but this can not yet be confirmed in Employer X’s case because the disclosures were not and would likely never be challenged in court.

The language in Employer X’s 204(h) notice resembles CIGNA’s disclosure language when it states that “In some cases, the new pension formula will provide a better pension benefit than would have been provided under the old formula.” Compare this with CIGNA’s, “…exact comparisons of benefits that cover all possible outcomes are difficult…[the plan] tends to provide larger benefits for shorter-service employees and comparable benefits for longer-service employees…” The nuance of the differences highlights CIGNA’s failure to convert their plan the way they wished. The content of Employer X’s notice is expressly vague whereas the language of CIGNA’s disclosure is vague yet it still implies substance. CIGNA’s ultimate surrender of their qualified plan to the terms of the federal government was less a result of their
omissions and more a result of their attempts to make affirmative statements regarding their new Qualified Plan. Their statements regarding “enhancements” “comparable benefits” and that “your benefit will grow steadily” were contrary to the substance and execution of the plan document and thus the plan document needed to be revised by the federal government to reflect these statements. No such affirmative statements were made by Employer X and therefore it is very likely that their disclosures, however inadequate, will go unchallenged given the very broad degree of freedom granted to the Plan Sponsor of the Qualified Plan by the Federal Government of the United States.

In summation, ownership of the Qualified Plan is maintained only if the IRS and DOL determine that the plan is not contrary to ERISA in form or execution and if the courts do not deem that the Plan Sponsor has inflicted injury upon participants. This latter point was illustrated by CIGNA’s court mandate to retroactively convert their “A or B” cash balance plan to an “A plus B” cash balance plan. This mandate demonstrates the Employer’s loss of ownership as a result of having done injury to the participant. Both aforementioned points are also illustrated by Employer X’s inadequate disclosure and how it passed a necessarily informal compliance test. The courts had no capacity to determine any inflicted injury and the IRS and DOL had not determined that the plan was contrary to ERISA in form or execution; therefore, Employer X’s ownership of the plan was maintained.
APPENDIX A:
ORIGINAL DATA
6. **Plan Administrator's Guide.** This memorandum is a brief description of some of the operational requirements applicable to maintaining the Plan, e.g., fiduciary bonding requirements, the trustee's fiduciary responsibility with respect to plan investments, limitations on annual additions and benefits, time for making employer contributions, etc. It is essential you understand the legal requirements applicable to maintaining the Plan.

7. **Administrative Forms and Memorandum on Use of Administrative Forms.** These forms are used for participants who become eligible for the Plan (Beneficiary Designation form) and for participants who terminate employment and wish to receive a distribution of their vested accrued benefit.

Please return the executed originals and executed copies of Items 1 - 4 to our office in the envelope provided.

The Plan that we have designed for you is a cash balance plan, which is considered by the Internal Revenue Service (the "IRS") to be an "individually designed plan". Under current IRS procedures and rulings, there are certain prescribed times when individually designed plan must be updated for various laws based on the last number of the adopting employers tax identification number. For Atlantic Advisors, this number is 4. Therefore, the Plan will be under the timing known as "Cycle D" for purposes of being updated for EGTRRA and any other current legislation. Therefore, sometime during the period which begins on February 1, 2009 and ends January 31, 2010, we will need to amend and restate the Plan and submit the Plan to the Internal Revenue Service for a favorable determination letter ruling. Sometime, during October or November of this year, the IRS will issue what is known as the "cumulative list" which details the various laws and language updates which must be included in the amended and restated plan. While I know that we will have contact before that time in the normal course of plan operations, I wanted you to be aware of this upcoming issue.

I greatly appreciate the opportunity to work with you on this project. If you have any questions, please do not hesitate to telephone me.

Very truly yours,
NOTICE TO ALL PLAN PARTICIPANTS
UNDER THE
CASH BALANCE PLAN
ISSUED – MAY 23, 2008

PURPOSE OF THIS NOTICE

will make several changes to our retirement benefits program under the Defined Benefit Plan, which will hereafter be called the Cash Balance Plan (the “Plan”). This Notice gives more specific detail regarding changes that will be made and how those changes might impact your retirement benefits. This Notice describes the new formula and how it affects the benefits you will earn in the future. In no event will your benefit be less than the benefit you have earned under the Plan as of June 9, 2008. However, depending on your circumstances, the benefit you earn under the new formula could be more or less than the benefit you would have earned under the Plan had it not been amended. This Notice is provided as required by Section 4980(F)(e) of the Internal Revenue Code of 1986 (the “Code”), as amended and Section 204(h) of the Employee Retirement Income Security Act of 1974 (“ERISA”), as amended.

OLD FORMULA

Through June 5, 2008, the generally applicable formula is a traditional formula that determined benefits based on your highest average pay and your years of Credited Service. Under the “old formula”, your annual benefit payable at your normal retirement date (defined as the later of the date on which you attain age 55 or the fifth (5th) anniversary of the first day of the plan year in which you commenced participation) was generally calculated as follows:

10% of your Average Compensation X your years of Credited Service
(Credited Service not to exceed 10 years)

DEFINITIONS OF ABOVE TERMS:

Average Compensation: the average of your compensation during the three (3) consecutive Plan years during your employment which produces the highest average.
Credited Service: the total plan years of service during which you complete 1,000 hours.

OLD FORMULA BENEFITS:

The benefit that you earned under the old formula will not be taken away from you. Instead, it will be frozen as of June 5, 2008. Your years of Credited Service and your Average compensation will also be frozen with respect to the old formula. If you have not earned a year of service during 2008, no benefit will accrue for 2008 under the old formula. Instead, you will receive benefits determined under the new formula as described below.

NEW FORMULA

The new pension formula that takes effect on January 1, 2008, provides a benefit calculated under a cash balance formula. This new cash balance benefit will be added to your frozen benefit earned under the old formula to determine your total benefit under the Plan.

Under the new cash balance formula, your cash balance benefit will be based on the value of your cash balance account. This is determined by:

- Contribution Credits based on your Total Compensation; and
- Interest Credits for each year until your benefit is paid to you.

OPENING CASH BALANCE ACCOUNT

The opening balance of your cash balance account on January 1, 2008 will be zero.

CONTRIBUTION CREDITS

Beginning on January 1, 2008, contribution credits will be added to your cash balance account at the end of each Plan year based upon the amount of your Total Compensation that you earned during the Plan year. Compensation is generally defined as your wages, salary, fees for professional services and other amounts received for personal services rendered in the course of employment. The amount of compensation the Plan may use for determining your contribution credits may be limited by the legal maximum set by the Internal Revenue Service ("IRS"). For 2008, the maximum amount if $230,000. If you terminate employment during the
Exhibit 4: page 3 of 204(h) notice

plan year, your contribution credits will be calculated based on your total compensation you earned during the plan year prior to your termination of employment.

INTEREST CREDITS

At the end of each plan year, your cash balance account will be credited with interest credits based upon the balance in your account on January 1 of such year. Your interest credits for a year are determined by multiplying your account balance on January 1 by the interest crediting rate for the plan year. The interest crediting rate is determined each year and is equal to the interest rate published.

No interest will be credited on December 31, 2008 because you did not have a cash balance account on January 1, 2008. Interest credits will first be added to your cash balance account on December 31, 2009 based on your cash balance account on January 1, 2009. If you terminate employment, your interest credits during the year of termination may be prorated.

COMPARING OLD AND NEW FORMULAS

In some cases, the new pension formula will provide a better pension benefit than would have been provided under the old formula. There may, however, be instances where the old formula would have provided a better benefit had it continued to apply.

If you have any questions, please do not hesitate to contact me.

Plan Administrator
4-5 SERVICE WITH PREDECESSOR EMPLOYER. If the Employer is maintaining the Plan of a Predecessor Employer, service with such Predecessor Employer is automatically counted for eligibility and vesting.

In addition, service with the following Predecessor Employers also will be counted for purposes of determining eligibility and vesting under this Plan, (See Sections 2.06 and 7.07 of the Plan.)

☐ (a) Identify Predecessor Employer(s): ________________________________

☐ (b) The following special rules apply:

[Use this (b) to impose limits on the service that will be taken into account with a Predecessor Employer for determining eligibility and vesting. For example, if service with a Predecessor Employer will not be taken into account in the same manner in applying eligibility and vesting, the limits applicable to such service may be identified in (b). Any limits imposed under this (b) may not cause the Plan to violate the nondiscrimination requirements under Treas. Reg. §1.401(a)(4).]

SECTION 5
COMPENSATION DEFINITIONS

5-1 TOTAL COMPENSATION. Total Compensation is based on the definition set forth under this AA §5-1. See Section 1.94 of the Plan for a specific definition of the various types of Total Compensation.

☐ (a) W-2 Wages

☐ (b) Code §415 Compensation.

☐ (c) Wages under Code §3401(a).

[For purposes of determining Total Compensation, each definition includes Elective Deferrals, pre-tax contributions to a Code §125 cafeteria plan or a Code §457 plan, and qualified transportation fringes under Code §132(f)(4).]

5-2 PLAN COMPENSATION. Plan Compensation is Total Compensation (as defined in AA §5-1 above) with the following exclusions described below.

☐ (a) No exclusions.

☐ (b) Elective Deferrals (as defined in Section 1.37 of the Plan), pre-tax contributions to a cafeteria plan or a Code §457 plan, and qualified transportation fringes under Code §132(f)(4) are excluded.

☐ (c) All fringe benefits, expense reimbursements, deferred compensation, and welfare benefits are excluded.

☐ (d) Compensation above $____ is excluded.

☐ (e) Amounts received as a bonus are excluded.

☐ (f) Amounts received as commissions are excluded.

☐ (g) Overtime payments are excluded.

☐ (h) Amounts received for services performed for a non-signatory Related Employer are excluded.

☐ (i) “Deemed §125 compensation” as defined in Section 1.94 of the Plan.

☐ (j) Amounts received after termination of employment are excluded (see Section 1.94 of the Plan).

☐ (k) Describe adjustments to Plan Compensation: ________________________________

SECTION 6
CONTRIBUTION CREDITS

6-1 CONTRIBUTION CREDITS. A Participant’s Cash Balance Account will be credited with the following Contribution Credits in accordance with Section 3.02(a) of the Plan. The Employer may elect different Contribution Credits for each designated group of Employees. In determining the Contribution Credits for a particular Employee group, only Eligible Participants in each Employee group are taken into account. (The Employer may designate additional Employee groups by adding an Addendum to this Agreement entitled “Designation of Employee Groups.”) In no event will the Contribution Credit for any Participant for any Plan Year exceed the Maximum Contribution Credit, as defined in Section 3.02(a)(2) of the Plan.

☐ (a) Group A: is the Owner and Managing Member

☐ (1) Each Eligible Participant in Group A for a particular Plan Year shall receive a Contribution Credit equal to ____% of his/her Plan Compensation for such Plan Year.

☐ (2) Each Eligible Participant in Group A for a particular Plan Year shall receive a Contribution Credit equal to $____ for such Plan Year.
(b) **Group B**: Is the spouse of the Owner and Managing Member.

|^ (1) Each Eligible Participant in Group B for a particular Plan Year shall receive a Contribution Credit equal to 100% of the Maximum Contribution Credit as specified in Section 3.02(a)(3) of the Plan, based on:
| ☐ the initial year of participation in the plan.
| ☑ each year of participation in the plan.

|^ (2) Each Eligible Participant in Group B for a particular Plan Year shall receive a Contribution Credit equal to $__ for such Plan Year.

|^ (3) Each Eligible Participant in Group B for a particular Plan Year shall receive a Contribution Credit equal to ___% of the Maximum Contribution Credit as specified in Section 3.02(a)(2) of the Plan, based on:
| ☐ the initial year of participation in the plan.
| ☑ each year of participation in the plan.

(c) **Group C**: is the Trading Principal.

|^ (1) Each Eligible Participant in Group C for a particular Plan Year shall receive a Contribution Credit equal to ___% of his/her Plan Compensation for such Plan Year.

|^ (2) Each Eligible Participant in Group C for a particular Plan Year shall receive a Contribution Credit equal to $__ for such Plan Year.

|^ (3) Each Eligible Participant in Group C for a particular Plan Year shall receive a Contribution Credit equal to ___% of the Maximum Contribution Credit as specified in Section 3.02(a)(2) of the Plan, based on:
| ☐ the initial year of participation in the plan.
| ☑ each year of participation in the plan.

(d) **Group D**: is the Business Development Principal.

|^ (1) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to ___% of his/her Plan Compensation for such Plan Year.

|^ (2) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to $__ for such Plan Year.

|^ (3) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to ___% of the Maximum Contribution Credit as specified in Section 3.02(a)(2) of the Plan, based on:
| ☐ the initial year of participation in the plan.
| ☑ each year of participation in the plan.

(c) **Additional groups**: Additional Employee group(s) and the Contribution Credits for such group(s) are described in an Addendum to this Agreement entitled “Designation of Employee Groups.”

### INTEREST CREDITS

A Participant’s Cash Balance Account will be credited with the Interest Credit designated in subsection (a) for the period designated in subsection (b). In applying the Interest Credit under this AA §6-2, a Participant’s Cash Balance Account is determined as of the first day of the period selected in subsection (b). (See Section 3.02(b) of the Plan)

#### (a) **Amount of Interest Credit.**

|^ (1) The Interest Credit for a particular period shall equal the rate of interest on 30-year Treasury Securities (as described in Code §417(e)(3)(A)(i)(I)) prior to amendment by the Pension Protection Act of 2006) as in effect for the month of December of the preceding Plan Year.

|^ (2) The Interest Credit for a particular period shall equal ___% of the Participant’s Cash Balance Account.

|^ (3) (Describe Interest Credit)

*[Note: As of the PPA Effective Date (as designated in AA §11-6), the Interest Credit designated under this AA §6-2 will not exceed a Market Rate of Return, as defined in Section 1.57 of the Plan. To the extent the Interest Credit designated under this AA §6-2 for any period exceeds a Market Rate of Return, the Interest Credit designated under this AA §6-2 for such period will automatically be reduced so that the Interest Credit equals a Market Rate of Return. See Section 3.02(b) of the Plan.]*
ADDENDUM
DESIGNATION OF EMPLOYEE GROUPS

☐ (e) Group E: Director of Marketing
☐ (1) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to 10% of his/her Plan Compensation for such Plan Year.
☐ (2) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to $________ for such Plan Year.
☐ (3) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to __% of the Maximum Contribution Credit as specified in Section 3.02(a)(2) of the Plan, based on:
☐ the initial year of participation in the plan.
☐ each year of participation in the plan.

☐ (f) Group F: Spouse of the Trading Principal
☐ (1) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to 50% of his/her Plan Compensation for such Plan Year.
☐ (2) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to $________ for such Plan Year.
☐ (3) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to __% of the Maximum Contribution Credit as specified in Section 3.02(a)(2) of the Plan, based on:
☐ the initial year of participation in the plan.
☐ each year of participation in the plan.

☐ (g) Group G: Senior Vice President of Trading
☐ (1) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to 0% of his/her Plan Compensation for such Plan Year.
☐ (2) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to $________ for such Plan Year.
☐ (3) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to __% of the Maximum Contribution Credit as specified in Section 3.02(a)(2) of the Plan, based on:
☐ the initial year of participation in the plan.
☐ each year of participation in the plan.

☐ (h) Group H: All other Employees
☐ (1) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to 7.5% of his/her Plan Compensation for such Plan Year.
☐ (2) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to $_______ for such Plan Year.
☐ (3) Each Eligible Participant in Group D for a particular Plan Year shall receive a Contribution Credit equal to __% of the Maximum Contribution Credit as specified in Section 3.02(a)(2) of the Plan, based on:
☐ the initial year of participation in the plan.
☐ each year of participation in the plan.
Exhibit 6: page 2 of the DB Adoption Agreement

Non-Standardized Non-Integrated Defined Benefit Pension Plan

6. EFFECTIVE DATE (a new Plan must choose a; a restated plan must choose b, c, d, e, and f are optional)
   a. [X] This is a new Plan effective as of January 1, 2004 (hereinafter called the "Effective Date").
   b. [ ] This is an amendment and restatement of a previously established qualified plan of the Employer which was originally effective ______ (hereinafter called the "Effective Date"). The effective date of this amendment and restatement is ______.
   c. [ ] FOR GUST RESTATEMENTS: This is an amendment and restatement of a previously established qualified plan of the Employer to bring the Plan into compliance with GUST (GATT, USEKRA, SEJPA and IRA '97). The original Plan effective date was ______ (hereinafter called the "Effective Date"). Except as specifically provided in the Plan, the effective date of this Plan is January 1, 2005. (May enter a restatement date that is the first day of the current Plan Year. The Plan contains appropriate retroactive effective dates with respect to provisions for the appropriate law.)
   d. [X] Amendment by page substitution. This is an amendment by substitution of certain pages of this Adoption Agreement.

   Identify the page(s) being replaced:
   Pages 8 and 12

   Effective Date of such changes:
   January 1, 2005

7. PLAN YEAR means the 12 consecutive month period:
   Beginning on January 1st ______ (e.g., January 1st)
   month    day
   and ending on December 31st ______
   month    day

   EXCEPT that there will be a short Plan Year:
   a. [X] N/A
   b. [ ] beginning on ______ (e.g., July 1, 2000)
      month    day, year
      and ending on ______
      month    day, year

8. PLAN NUMBER assigned by the Employer
   a. [X] 001
   b. [ ] 002
   c. [ ] 003
   d. [ ] Other ______

9. TRUSTEE(S):
   a. [ ] N/A. The Plan is fully insured.
   b. [X] Trustee(s)

      1. [X] Name(s)               Title(s)
         Bennet Sedacca                Trustee


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SECTION 3

ACCRUED BENEFITS

3.01  **Accrued Benefit.** A Participant’s Accrued Benefit under the Plan, as of any date, shall be the balance in his/her Cash Balance Account determined as of such date. Notwithstanding any provision of the Plan to the contrary, a Participant’s Accrued Benefit, as of any given date of determination, must be greater than or equal to the Accrued Benefit of any similarly situated younger individual who is or could be a Participant. For purposes of this provision, a Participant is similarly situated to any other individual if such Participant is identical to such other individual in every respect (including period of service, compensation, position, date of hire, work history and any other respect) except for age.

3.02  **Cash Balance Account.** A Cash Balance Account will be maintained for each Participant. The Cash Balance Account is a notional account and is used to determine the amount of retirement benefit payable under this Section 3.02. A Participant’s Cash Balance Account shall equal the sum of the Contribution Credits (as determined in subsection 3.02(b) below) and the Interest Credits (as determined in subsection 3.02(b) below). The Participant shall not have an actual Account and shall have no claim to any particular assets of the Plan.

(a)  **Contribution Credits.** For each Year of Accrual Service, a Contribution Credit will be credited to the Cash Balance Account of each Eligible Participant in accordance with this subsection 3.02. Contribution Credits will be credited as of the last day of the Plan Year in the amount specified by the Employer under AA §6-1.

(1)  **Percentage of Plan Compensation or Designated Dollar Amount.** The Employer may elect under AA §6-1 to provide Eligible Participants in the selected Employee group with a Contribution Credit that is determined as a uniform percentage of Plan Compensation for the Plan Year or as a uniform dollar amount.

(2)  **Maximum Contribution Credit.** The Employer may elect under AA §6-1 to provide Eligible Participants in the selected Employee group with the Maximum Contribution Credit or a percentage of the Maximum Contribution Credit as specified in the Agreement. For this purpose, the Maximum Contribution Credit for any Eligible Participant in the selected Employee group is equal to 10% of the actuarial present value of the Defined Benefit Dollar Limitation applicable to the Participant for the Plan Year, based on the Participant’s attained age, in completed years, on the last day of the Plan Year. For this purpose, the Defined Benefit Dollar Limitation shall be determined using the greater of 6% or the Applicable Interest Rate and the Applicable Mortality Table.

(3)  **Minimum Benefit.** The Employer may elect under AA §6-4 to provide a minimum Contribution Credit to Eligible Participants designated under the Agreement. The minimum Contribution Credit may be defined as a specified dollar amount, a specified percentage of Plan Compensation or as the dollar amount necessary to provide a Meaningful Benefit (as defined in Section 1.59).

(b)  **Interest Credits.** Interest Credits shall be credited to the Cash Balance Account of each Eligible Participant who has a Cash Balance Account under the Plan based upon the elections under AA §6-2. Interest Credits will be determined based on the amount of a Participant’s Cash Balance Account as of the period elected under AA §6-2(b). Interest Credits will be added to each Participant’s Cash Balance Account as of the last day of the period elected under AA §6-2(b). However, for any period in which a Plan distribution is made to a Participant, interest shall be credited on the amount of the Participant’s Cash Balance Account as of the first day of the applicable period through the end of the month preceding the month in which the distribution is made. In no event will Interest Credits continue to be credited on any portion of the Cash Balance Account that has been distributed to the Participant or Beneficiary nor will the Interest Credits for a Plan Year cause the Cash Balance Account as of the last day of the Plan Year to be less than the accumulated contributions as of the last day of the Plan Year.

As of the PPA Effective Date (as defined in Section 1.75), a Participant will not be credited with an Interest Credit for any period that exceeds a Market Rate of Return (as defined in Section 1.57). If for any period beginning on or after the PPA Effective Date, an Interest Credit designated under the Plan exceeds a Market Rate of Return, the Interest Credit automatically will be reduced for such period to the extent necessary to provide an interest rate equal to the rate of interest on 30-year Treasury securities (as described in Code §417(e)(3)) prior to amendment by the Pension Protection Act of 2006).

3.03  **Offset of Benefits – Defined Contribution Plan.** The vested portion of the Accrued Benefit that would otherwise be payable to a Participant under the Plan may be reduced (but not below zero) by the vested portion of a Participant’s Account Balance attributable to Employer Contributions (plus the Actuarial Equivalent of any prior distributions from such Account) under a Defined Contribution Plan maintained by the Employer (as designated under AA §6-5(a)). For purposes of determining the Actuarial Equivalence of distributions under the Defined Contribution Plan, no mortality assumptions shall be applied for purposes of determining the Actuarial Equivalence of any distributions for periods prior to the commencement of benefits under this Plan.
Exhibit 8: Employee Census

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<th>DATES</th>
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</tr>
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</table>

* EMPLOYEE WORKED MORE THAN MINIMUM HOURS REQUIRED FOR CONTRIBUTION

PS=Past Service  FS=Future Service  PA=Participation Age  AA=Attained Age  RA=Retirement Age
Exhibit 9: page 8 of the DB Adoption Agreement

Non-Standardized Non-Integrated Defined Benefit Pension Plan

to be taken into account shall be ___.

e. [X] 10% of Average Compensation, multiplied by the first 10 years of Credited Service

   1. [ ] plus ___% of Average Compensation multiplied by the next ___ years of Credited Service
   2. [ ] plus ___% of Average Compensation multiplied by the number of all remaining years of Credited Service.

   The maximum number of years of Credited Service to be taken into account shall be ___.

NOTE: If the unit accrual method applies, any percentage selected in 1. or 2. above may not be more than 133 1/3% greater than any prior percentage under the formula. If the Employer elects to apply the Fractional Accrual Method and the years of Credited Service to which the first percentage under e. applies is less than 33, special limits apply for the Plan to qualify as a safe harbor plan under the Code Section 401(a)(4) Regulations.

f. [ ] Accumulation Plan. The benefit formula selected under c. or e. applies separately for each Plan Year, using Compensation for the Plan Year (instead of Average Compensation).

22. REDUCTIONS AND LIMITATIONS Regardless of the above, the formula above will be modified as follows (select all that apply):

   a. [X] No reductions or limitations.
   b. [ ] A Participant's benefit shall be reduced on a pro-rata basis for each year of Credited Service less than ___ (e.g., 25) that the Participant is credited with at Normal Retirement Date.
   c. [ ] A Participant's benefit shall not exceed ___.
   d. [ ] A Participant's benefit shall not be less than ___.
   e. [ ] Increases in a Participant's benefit resulting from a change in Compensation shall be recognized as of each Anniversary Date, but decreases shall not be recognized until the decrease in Compensation has been in effect for ___ Plan Years.
   f. [ ] The benefit shall be rounded to the [ ] nearest ___.

NOTE: To be a safe harbor plan under the Section 401(a)(4) Regulations, if a fractional accrual method is used with a Flat Benefit formula, option b. above must be selected with a reduction for Credited Service less than 25.

23. CREDITED SERVICE (Plan Section 1.17) for purposes of applying the benefit formula means, with respect to a Participant:

   a. [X] N/A. The retirement benefit formula is not based on Credited Service.
   b. [X] Total Years of Service (as defined for benefit accrual purposes).
   c. [ ] Plan Years of Service (as defined for benefit accrual purposes).

AND, if a fractional accrual method is NOT being used, then the following limitations apply in determining Credited Service (select all that apply):

   d. [X] No limitations.
   e. [ ] Credited Service completed prior to ___ (or ___) is disregarded.
   f. [ ] Credited Service attributable to "past service credit" shall be limited to ___ years (the safe harbor is 5 years or less). "Past service credit" means (A) benefit accruals for service prior to the Effective Date of this Plan, (B) increases in existing Accrued Benefits resulting from service prior to the Effective Date of a Plan amendment, and (C) benefit accruals for service with another employer.

NOTE: To be a safe harbor plan under the Section 401(a)(4) Regulations, if a fractional accrual method is being used, Credited Service and service used in the fraction must be determined on the same basis.

24. ACCRUED BENEFIT (Plan Section 1.1) shall be:

   a. [X] Calculated using the...
   1. [X] 133 1/3% rule (unit accrual).
   2. [ ] Fractional rule based on Years of Service.
   3. [X] Fractional rule based on Plan Years of Service.
   4. [ ] Fractional rule using Plan Years of Service, plus ___ Years of Service credited prior to Plan entry.
   5. [ ] 3% rule.
   6. [ ] N/A. Plan is fully insured (i.e., a Code Section 412(i) plan).
APPENDIX B: UNDEFINED TERMS
(All definitions are reproduced verbatim from Sal Tripodi’s *The ERISA Outline Book 2011 Edition* with the exception of Highly Compensated Employee which is paraphrased)

**Alternate Payee**— May be a spouse, a former spouse, or a child or other dependent of the participant, “who is recognized by a domestic relations order as having a right to receive all, or a portion of, the benefits payable under the plan with respect to the participant.”

**Employee**— A common law employee as determined under common law employer-employee principles, who is or was employed by the employer that maintains the plan, or a self-employed individual with respect to the trade or business that maintains the plan.

**Employer**— The employer is any employer (under common law principles) of the employees covered by the plan. Only an employer may establish a qualified plan, and the plan must be exclusively for the benefit of the employees (or former employees) of the employer and the beneficiaries of those employees or former employees. The IRS maintains that a plan ceases to be a qualified plan if the sponsoring employer goes out of business, unless a successor employer takes over sponsorship of the plan.

**Fiduciary**— A person is a fiduciary if he is described in A., B. or C. below.

A. **Management.** The person exercises any discretionary authority or discretionary control respecting management of the plan, or exercises any authority or control respecting management or disposition of assets.
B. Investment advice. The person renders investment advice for a fee or other compensation, direct or indirect, with respect to any assets of the plan, or has any authority or responsibility to render such advice even if not actually rendered.

C. Administration. The person has any discretionary authority or discretionary responsibility in the administration of the plan.

**Highly Compensated Employee**— An employee is an HCE for a plan year if the employee meets one of two tests: the five-percent owner test or the compensation test. The five-percent owner test is if the Employee owns more than 5% of the Employer including attributed ownership. The compensation test is if the employee received—during the previous year—more than a dollar amount indexed for cost of living adjustments. This amount was $105,000 during 2008.

**Participant**— A participant is an employee or former employee who is covered by the plan.

**Plan Administrator**— The plan administrator is the person designated to be responsible for the administration and operation of the plan and, as such, is a named fiduciary with respect to the plan. The plan administrator is the person identified as the administrator in the plan document.
**Plan Document**— The written document setting forth the terms of the plan, including the eligibility and vesting requirements, how benefits are determined, and when benefits may be distributed.

**Qualified Domestic Relations Order ("QDRO")**— A domestic relations order that provides for the payment of all or a portion of the participant's benefits to an "alternate payee".

**Vested**— An ownership right in the benefits under the plan. The term nonforfeitable is also used interchangeably with the term vested. An employee's vested accrued benefit is the portion of the accrued benefit that cannot be forfeited except under very limited circumstances.
REFERENCES

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of New York 2003).
Brown, Kyle N. (2011). Specialized Qualified Plans – Cash Balance, Target, Age-Weighted and
CIGNA Corp. v. Amara, 131 S. Ct. 1866 (Supreme Court 2011).
Connecticut 2008).
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Klosterman v. Western General Management, Inc., 32 F.3d 1119 (U.S. 7th Circuit Court of Appeals, 1994).


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Kathi Cooper v. IBM Personal Pension Plan, 457 F.3d 636 (U.S. 7th Cir. Court of App., 2006).


Sunder v. U.S. Bancorp Pension Plan, 586 F.3d 593 (8th Circuit, 2009)
