Court Challenges to DB Plan Actuarial Assumptions – One Year Later

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Eleven cases have been filed against defined benefit pension plan sponsors and certain fiduciaries alleging that the plan's assumptions—called "actuarial equivalence factors" or "actuarial equivalence assumptions"— for converting a single-life annuity (the default form of benefit under ERISA) to an optional form of benefit, such as a joint-and-survivor annuity or a certain-and-life annuity, are unreasonable, result in lower benefits than what plaintiffs are entitled to, and therefore violate ERISA. In some cases, the plaintiffs have similarly claimed that the plan's early retirement reduction factors are unreasonable. The plaintiffs often are specifically targeting the use of older mortality tables (*e.g.*, 1971 and 1983 tables), or other reduction factors, which plaintiffs argue are outdated and produce smaller benefits for participants. The plaintiffs in these cases seek the difference between their current plan benefits and the benefits they would have received if their benefit was calculated using more "current" interest rate and mortality assumptions (usually measured by the assumptions the Internal Revenue Code requires for the purpose of, *inter alia*, calculating lump sum benefits).

Motions to dismiss have been filed in all but one case, *Brown et al. v. United Parcel Service of America, Inc.*, filed on January 31, 2020. While the defendants' arguments vary from case-to-case, they generally include positions that (1) ERISA does not impose a "reasonableness" requirement with respect to the actuarial equivalence factors, (2) plaintiffs lack standing to enforce the Treasury regulations imposing a "reasonableness" requirement, (3) plaintiffs have not alleged and/or cannot establish that the existing plan factors are outside the range of reasonableness, (4) plaintiffs' claims are time-barred, and (5) as to plaintiffs' fiduciary breach claims, the adoption of actuarial equivalence assumptions is a settlor, and not a fiduciary, function.

The courts in *Torres v. American Airlines, Inc.* (N.D. Tex.), *Smith v. U.S. Bancorp* (D. Minn.), *Cruz v. Raytheon Company* (D. Mass.), *Belknap v. Partners Healthcare System, Inc.* (D. Mass.), and *Smith v. Rockwell Automation, Inc.* (E.D. Wis.) denied defendants' motions to dismiss in those cases. However, the courts' reasoning for doing so has varied. Some courts appear to agree with plaintiffs that while the actuarial equivalence requirements under ERISA do not expressly include a "reasonableness" requirement, Treasury regulations, which do require the use of reasonable assumptions, are enforceable by participants under ERISA. Other courts more generally allow for the possibility that ERISA's actuarial equivalent requirement implicitly includes a reasonableness standard apart from the Treasury regulations. The *Cruz* and *Smith* courts noted, however, that reasonableness is a zone, and not a point. The *Smith* court also rejected defendants' argument that reasonableness is ascertained as of the date the assumptions were adopted, so that even if the assumptions later became unreasonable, the plan sponsor would not be obligated to amend the plan. Instead, the court said that a sponsor is required to update its plan with reasonable assumptions, even if that has the effect of continually increasing benefits.

In any event, these courts held that the plaintiffs met their pleading burdens, and that the factual record needs to be developed to resolve whether the actuarial equivalence factors at issue violate ERISA. On the other hand, the *Belknap* court rejected the argument that ERISA's actuarial equivalence requirements be based on "reasonable" actuarial assumptions, and instead ordered supplemental briefing on the meaning of "actuarial equivalence".

While most of the courts that have ruled on the motions to dismiss have denied them, the district court granted the defendants' motion in *DuBuske v. PepsiCo, Inc.* (S.D.N.Y.) on the grounds that the plaintiffs retired before normal retirement age and did not allege that they were deprived of their normal retirement benefits at normal retirement age. The plaintiffs asked the court to reconsider its ruling, and the court gave the opportunity for plaintiffs to file an amended complaint. It appears that the case settled shortly thereafter.

While many of these cases are still awaiting a decision from the court on defendants' motions to dismiss, the defendants in *Herndon v. Huntington Ingalls Industries, Inc.* filed a motion for summary judgment following discovery, arguing that (1) there is no legal requirement that the actuarial equivalent factors be updated, (2) the assumptions are plan terms that have been collectively bargained and therefore cannot be changed without union agreement, (3) reasonableness is a range and the plan's factors are within the range of reasonableness, and (4) the plan's conversion factors provide a higher benefit than the factors used by both plaintiffs' and defendants' experts. The plaintiff opposed the motion, arguing that the plan's actuarial factors are unreasonable (contrary to defendants' expert's opinion) and must be updated to produce actuarially equivalent benefits at the time the benefits are calculated. The plaintiff further argues that bargaining parties' agreement cannot override ERISA's actuarial equivalence requirements. The Court has yet to rule, and presumably the defendants will reply.

GROOM INSIGHT. Given that some complaints have survived motions to dismiss, the lack of controlling guidance, and limited legal precedent in this area, there certainly remains risk of exposure for pension plan sponsors. As external legal counsel with extensive defined benefit plan experience and actuarial knowledge, Groom is well-positioned to assist plan sponsors in evaluating potential risks and possible proactive steps to minimize any risk.