

April 23, 2010

MEMORANDUM TO CLIENTS

RE: Supreme Court Decision in *Conkright v. Frommert*

The Supreme Court's April 21, 2010 decision in *Conkright v. Frommert* upholds the continuing vitality of deference owed to an ERISA plan administrator as established in *Firestone v. Bruch*. In light of recent widespread attacks on discretionary clauses in ERISA plans, the decision is a welcomed relief. The bottom line? Deference cannot be stripped away simply because a plan administrator made a mistake in interpreting the terms of the plan.

Background: The "Mistake"

In *Conkright*, plan participants retired from the employ of a plan sponsor and received lump-sum distributions of retirement benefits. The plan sponsor rehired the employees many years later. Their return required the administrator to calculate the impact of the lump-sum distributions on current benefits. Significantly, the underlying ERISA plan gave the administrator discretion to interpret plan terms.

The administrator applied a so-called "phantom account" method to account for the past distributions. The objective of the "phantom account" method was to replicate the market experience of a defined sum of money over a fixed time period. Here, the methodology essentially would replicate the market experience of the lump-sum distributions during the participants' period of retirement.

In a lawsuit filed in the Western District of New York, the participants argued that the methodology was unreasonable and that they did not receive adequate notice that it would be applied. The method that the plan administrator used in calculating benefits did not withstand review. After surviving deferential review in the District Court, the Court of Appeals for the Second Circuit remanded the matter for a new determination of the participants' benefits under the terms of the plan.

Review of Decision on Remand

Dissatisfied with a new interpretation of the plan proposed by the administrator on remand before the District Court, the plaintiffs pressed for a different interpretation. In turn, the District Court did not defer to the plan administrator's new interpretation of the plan, or to the administrator's proposed methodology for calculating benefits. Instead, the District Court adopted a separate calculation. The District Court's methodology did not account for the time value of money, and thus substantially reduced the impact of the lump-sum distributions on current benefits.

The Court of Appeals for the Second Circuit affirmed the District Court's decision. In so doing, the Second Circuit created an exception to the fundamental ERISA rule that an administrator is entitled to deference if the plan confers upon the administrator discretion to

interpret plan terms. According to the exception, an administrator that errs in interpreting the plan in the first instance is no longer entitled to deference upon re-interpreting the same plan terms. To use a baseball analogy, for plan administrators it's "one-strike-and-you're-out."

Result: The Supreme Court Reverses

The Supreme Court rejected the Second Circuit's "one-strike-and-you're-out" analysis and held that the District Court should have deferred to the plan administrator's new interpretation of the plan on remand. The Court reasoned that a single mistake was insufficient to strip a plan administrator of deference otherwise owed.

In reversing the Second Circuit, the Court reviewed the seminal cases of *Firestone* and *MetLife v. Glenn*. According to the Court, *Firestone* left no room for the creation of ad hoc exceptions to the deferential standard of review. The Court further reasoned that, if, under *Glenn*, the standard of review remains intact even when the administrator operates under a conflict of interest, then an administrator should not be stripped of deference after simply making a mistake. While an administrative decision may not be entitled to deference if the administrator exercises discretion unfairly, incompetently, or in bad faith, a good-faith error should not result in a similar loss of deference. The Court expressed concern that a contrary ruling could disrupt national uniformity of plan administration because courts would interpret the terms of a plan *de novo* every time an administrator's interpretation was found to be mistaken or unreasonable. Simply put, ERISA is far too complicated to require perfect first efforts. Rather, deferential review should be accorded even after an initial, good-faith error.

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