THE WAGNER LAW GROUP

A PROFESSIONAL CORPORATION

Legal Updates in the ERISA & Employee Benefits World

ERISA, Employee Benefits and Executive Compensation Law

October 2010

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Marcia Wagner

Recently Presented Seminars

Below is a link to seminar material that Marcia has recently presented.

"What You Need to Know About Health Care Reform Compliance," HighRoads, Inc., September 16, 2010

"**What is New in DC: The Most Critical Items to the Obama Administration**," Putnam Investments for National Retirement Partners, July 29th in Boston

Recently, there have been several high profile litigation matters and rulings. This Newsletter addresses issues and changes in regards to same sex marriage, excessive fee claims and attorney fees, as well as other matters.

If you have any questions or seek our counsel, please contact any of The Wagner Law Group attorneys, specialists in ERISA, employee benefits and executive compensation law.

To learn more about our team and practice, please visit our website at www.erisa-lawyers.com.

Best Regards,
Marcia Wagner

Litigation Matters

Same Sex Marriage Matters

1. Defense of Marriage Act Declared Unconstitutional in Massachusetts - The Defense of Marriage Act ("DOMA") was declared unconstitutional by a Federal District Court judge in Massachusetts. DOMA states that for purposes of interpreting any federal law that a person will not be considered married unless the spouse is of the opposite sex. The decision, Gill & Letourneau v. Office of Personnel Management, will most likely be appealed by the Department of Justice, and President Obama has expressed Congress should repeal DOMA.

Judge Tauro held: "DOMA fails to pass constitutional muster even under the highly deferential rational basis test.... This court is convinced that there exists no fairly conceivable set of facts that could ground a rational relationship between DOMA and a legitimate government objective. DOMA, therefore, violates core constitutional principles of equal protection." Currently, benefit administrators should not change their employee benefit plans in Massachusetts in light of this ruling, as it will be appealed. Since this is not a final decision, it is still necessary for federal purposes (the Internal Revenue Code and ERISA) to administer benefit plans with special "same-sex" rules, as follows:

o For health plans, it is required to impute federal taxable wages to an employee equal to the "value" of a same-sex spouse's coverage, unless the same-sex spouse qualifies as a federal health care dependent, i.e., has the same principal abode as the employee for the year and receives more that 50% support from the employee. The IRS has not opined on "value" for this purpose, so the standard approach is to impute the single premium COBRA cost.

o There is no imputed Massachusetts taxable income to employees who have same-sex spouses.

Articles Published

Below is a link to a recently published article written by Marcia Wagner.

"Lifetime Income Options," ***401(k) Advisor***, August 2010

TV Appearances

Below is a link to a recent television appearance by Marcia Wagner on the Fox Business Network.

Fox Business Network - The Willis Report, U. S. Wants to Help You Save For Retirement, September 13, 2010

Webinars & Podcasts

"What You Need to Know About Health Care Reform Compliance," HighRoads, Inc., September 16, 2010
- ***View Marcia Wagner's webinar here***

"ERISA Litigation Update," Marcia Wagner, August 13, 2010, BigMediaUSA.com
- ***Listen to Marcia Wagner's podcast here***

Quoted Articles

Marcia has been quoted in a number of publications.

"Worker Contributions to U.S. Health Premiums Jump 14%, Kaiser Survey Says," ***Bloomberg.com***, September 2, 2010

"Target Date Turnover Troubles Big Firms," ***Investment News,*** August 29, 2010

"SEC's Target Date Proposal Met With Raging Indifference,"***Investment News***, August 20, 2010

"Exercising Fiduciary Authority and Control Over the Investment Menu in ERISA 403(b) Plans,"***Plansponsor.com***, August 3rd

"Legislation Could Limit Use of Swaps,"***Employee Benefit News***, August 1st

"Employee Suits Alleging Excessive 401(k) Fees Gain Ground," ***Los Angeles Times***, July 28th

o For Section 125 cafeteria plans with medical and dental reimbursement accounts, no reimbursement is allowed for a same-sex spouse, unless the spouse qualifies as a federal health care dependent.
o For FMLA, there is no federal right to unpaid leave to care for a same-sex spouse.

2. California's Ban on Same-Sex Marriage Held Unconstitutional - The U.S. District Court of the Northern District of California rules that California's ban on same-sex marriage (Proposition 8) is unconstitutional because it denies same-sex couples the right to due process and equal protection of the laws as guaranteed by the Fourteenth Amendment to the U.S. Constitution. Same-sex marriage was legalized in California in June 2008 after the California Supreme Court ruled that state laws limiting marriage to opposite-sex couples violated the state constitutional rights of same-sex couples. However, same-sex marriage was banned in the state a few months later after voters approved Proposition 8, an amendment to the California constitution that prohibits the state from legally recognizing same-sex marriages performed on or after November 5, 2008. The validity of Proposition 8 under the state constitution was upheld by the California Supreme Court in June 2009. Although the ruling banned same-sex marriage going forward, the 2009 ruling notably held that more than 18,000 same-sex marriages performed in the state during the nearly five months that it was legal would continue to be valid and recognized for all purposes of state law. The recent case, Perry v. Schwarzenegger, was filed by the American Foundation for Equal Rights on behalf of two same-sex couples who were denied the ability to marry after the passage of Proposition 8. This case was the first federal challenge to state laws banning marriages between same-sex couples. In finding that Proposition 8 violates the U.S. Constitution, the District Court held that the ban on same-sex marriage "fails to advance any rational basis in singling out gay men and lesbians for denial of a marriage license." The defendants, immediately filed an appeal with the Ninth Circuit Court of Appeals and requested that the District Court grant a stay of its decision pending the outcome of the appeal. The Ninth Circuit granted the stay, thus temporarily blocking same-sex marriages from resuming in California. However, the Appeals Court set a "fast track" schedule to hear the merits of the constitutional challenge to Proposition 8. Thus, it is not clear whether and when same-sex couples will be able to marry again in California. Regardless of the outcome of the appeal, the case is expected to be appealed to the Supreme Court of the United States.

Currently, 40 states have enacted laws or approved constitutional amendments banning same-sex marriage. Same sex marriage is currently legal in five states and in the District of Columbia, while civil unions are permitted in New Jersey. The five states are Massachusetts, Connecticut, Vermont, Iowa, and New Hampshire.

Given this matter is far from over, benefits administrators should only do the minimum necessary to comply with the California law limiting same-sex marriages to those that occurred during the short period in which same-sex marriage was legal; this would include reviewing employee benefits plans to determine whether changes are necessary. Employers may need to revise eligibility descriptions in summary plan descriptions ("SPDs") and enrollment forms to address the types of same-sex marriages eligible for spousal benefits. In addition, employers will have to be careful and specific in defining the term "spouse" in their benefit plan documents and SPDs.

Court Ruling on Excessive Fee Claim Against Mutual Fund Investment Advisor May Have Implications for 401(k) Excessive Fee Cases

The Supreme Court recently ruled in Jones v. Harris Associates L.P. that fees paid to a mutual fund's investment advisor will not violate the advisor's fiduciary duty under the Investment Company Act of 1940 (the "Act"), unless the fees are so disproportionately large that they could not have been the product of arm's-length bargaining. This decision may have an affect on plans and fiduciaries defending the rash of litigation under ERISA involving allegations of excessive fees charged by service providers under 401(k) plans.

1. Background - The Act creates protections for mutual funds and their shareholders against potential abuses by the mutual funds' investment advisors.

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The Wagner Law Group Description

The Wagner Law Group, A Professional Corporation, is a nationally recognized ERISA, employee benefits, executive compensation and employment firm.

Established in 1996, The Wagner Law Group has 15 attorneys engaged exclusively in employee benefits law. The firm is among the largest ERISA boutiques in the country. The practice is national in scope, with clients in more than 30 states and several foreign countries.

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Among other requirements, under Act Section 36(b), an investment advisor is subject to a fiduciary duty with respect to the fees it charges the fund for its services. The Act also requires that a board of trustees be appointed to oversee the fund annual review and approve the contract with the advisor and the advisor's compensation from the fund.

The plaintiffs in Jones, shareholders in mutual funds managed by the defendant investment advisor, filed suit derivatively on behalf of the funds, claiming that the defendant breached its fiduciary duty under the Act with respect to the amount of compensation it charged the fund. Although the defendant charged fees comparable to the fees that other investment advisors charged similar mutual funds, the fees were nearly twice the amount that the advisor charged institutional clients for similar services. The U.S. District Court for the Northern District of Illinois concluded that the proper standard for adjudicating an investment advisor's breach of fiduciary duty under the Act was set forth by the U.S. Court of Appeals for the Second Circuit in Gartenberg v. Merrill Lynch Asset Management. Under the Gartenberg standard, an investment advisor breaches the advisor's fiduciary duty under the Act if the fee it charges the fund is so disproportionately large that it bears no reasonable relationship to the services rendered and could not have been the product of arm's-length bargaining in light of all the surrounding circumstances. After reviewing the fees that the defendant received from the funds, the fees the defendant charged to other clients and the fees that other investment advisors charged similar mutual funds, the district court concluded that the amount of fees at issue did not raise a triable issue under the Gartenberg standard and granted summary judgment for the investment advisor.

On appeal, the Seventh Circuit affirmed the district court's judgment in favor of the investment advisor, but rejected Gartenberg's standard under which such breach of fiduciary duty claims should be adjudicated. Instead, the Seventh Court concluded that an investment advisor breaches the advisor's fiduciary duty under the Act only if the advisor fails to fully disclose the facts relevant to its fees to the fund's board of trustees. An analysis of the advisor's compensation from the fund is only relevant under the Seventh Circuit's standard if it is so unusual that it raises an inference that fraud or deceit must have occurred or that the fund's board of trustees failed to engage in an arm's-length negotiation of the fees.

2. Supreme Court's Decision - Writing on behalf of a unanimous court, Justice Alito rejected the Seventh Circuit's standard of full disclosure and instead embraced Gartenberg as the correct standard for adjudicating whether an investment advisor breached the advisor's fiduciary duty to mutual fund shareholders under the Act. In doing so, the Supreme Court noted that Gartenberg has been the workable standard that a majority of the lower courts have followed in such cases for nearly 30 years.

The court concluded that the Gartenberg decision accurately reflects the compromise that is embodied in Section 36(b) of the Act between protecting mutual fund shareholders from fee arrangements that are not negotiated at arm's-length while simultaneously shifting the burden of proving that the investment advisor breached the advisor's fiduciary duty to the party alleging the breach.

In evaluating an investment advisor's compliance with the fiduciary duty under the Act, the Court noted that the Act does not require the courts to engage in a precise calculation of the fees that would result from arms-length negotiations between the advisor and the mutual fund's board of trustees. Comparisons between the amount of the challenged advisor's fees from the fund and the fees that the advisor charges other clients for investment advisory services may be relevant, provided that such comparisons consider the similarities and differences between the services the advisor provides to the mutual fund and those it provides other clients.

The court concluded that any assessment of the reasonableness of the investment advisor's fees must take into account the procedural safeguards of Act Section 36 (b) which require the fund's board of trustees to annually review and approve the fund's contract with the advisor and the amount of the advisor's compensation. Justice Alito cautioned that courts should not second guess the decisions of a mutual fund's board of trustees. Rather, courts should defer to the decisions of the board of trustees if the decisions are the result of a process for reviewing and approving the amount of the advisor's compensation from the fund. Judicial may be imposed on you or any other person under the Internal Revenue Code.

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scrutiny of the fee arrangement is, however, required if a court concludes that the board's process was deficient or if the advisor failed to disclose relevant information to the board, such that the board was unable to make an informed decision.

3. Impact on Plan Sponsors and Fiduciaries - Although the court's ruling in Jones is limited to claims of an investment advisor's breach of fiduciary duty under the Act with respect to the fees it charges to a mutual fund for its services, the decision may lend support for courts to apply the Gartenberg standard to excessive fees cases brought under ERISA. The Second Circuit has already concluded that Gartenberg is the correct standard to adjudicating a breach of fiduciary duty claim with respect to excessive fees under ERISA in Young v. General Motors. In light of the court's ruling in Jones, more courts may be willing to follow the Second Circuit's lead in applying the Gartenberg standard in the ERISA context, which will lead to greater deference to fee arrangements made by plan sponsors and fiduciaries provided they engage in a duly diligent process to ensure such fees are reasonable and negotiated at arm's-length.

Note: Plan sponsors should be working with their financial advisors to determine the amount of direct and indirect fees charged to their plans and the reasonableness of the fees in respect to the services provided. There is much litigation in this area and it is important fiduciaries are mindful of their duties to pay only reasonable fees.

Supreme Court Ruling on Attorney's Fees

In May, the Supreme Court ruled that a court may award an ERISA litigant attorney's fees even if he or she does not prevail.

In Hardt v. Reliance Standard Ins. Co., the Supreme Court ruled that a plan participant seeking disability benefits who had only succeeded in persuading the district court to remand for a more thorough review by the plan administrator, instead of obtaining a judgment awarding her benefits, had nevertheless achieved sufficient success to justify the district court's award of attorney's fees.

The participant, Ms. Hardt, an executive assistant, received disability benefits from her employer's insured plan for about two years before the insurance company, Reliance, concluded that she was no longer totally disabled under the terms of the plan. When Ms. Hardt appealed the termination of her benefits, Reliance referred Ms. Hardt for a functional capacities evaluation, had a physician review her records, and sought input from a vocational rehabilitation counselor, but ultimately concluded that the decision to terminate her benefits was correct.

When Ms. Hardt sued, the district court found that each of the reviews conducted by Reliance was flawed in some fashion. Although it found "compelling evidence" that Ms. Hardt was in fact totally disabled, the court did not award her benefits. Instead, citing Reliance's inadequate review, it remanded the case to Reliance.

Reliance again performed the review and found that Ms. Hardt was, in fact, disabled. Ms. Hardt then moved for an award of attorney's fees and costs under ERISA Section 502(g)(1), which authorizes a court to award, in its discretion, a "reasonable attorney's fee and costs of action to either party" in most types of ERISA cases. The district court concluded that Ms. Hardt was in fact a prevailing party because the remand order materially changed the relationship between Ms. Hardt and Reliance, and went on to find that an award of fees and costs in the amount of $39,149 was appropriate.

Reliance appealed, and argued that Ms. Hardt was not a prevailing party, and was therefore not entitled to fees. The Fourth Circuit agreed, ruling that a party must receive an "enforceable judgment on the merits" or a "court ordered consent decree" to be considered a prevailing party entitled to attorney's fees.

Ms. Hardt then petitioned the Supreme Court for relief. Writing for the Court, Justice Thomas noted that the plan language of ERISA Section 502 does not require a party to "prevail" to receive a fee award, but instead allows a court to award fees to either party, in its discretion. Thus, the Court held, a court may not introduce a "prevailing party" requirement in deciding whether a to award attorney's fees in an ERISA case. Instead, the Court held, a court should look to principles that have developed under other fee-shifting statutes that do not require prevailing party status. A fees claimant, the Court ruled, must show "some degree of success on the merits," a requirement that is not satisfied by a "trivial success" or a "purely procedural victory." In the case at hand, the Court held Ms. Hart's successes were neither trivial nor purely procedural, and the district court's award of attorney's fees was a proper exercise of discretion.

Note: This case may make it somewhat easier for plaintiffs to collect attorney's fees in ERISA cases.

Supreme Court Rules on Deferential Standard of Review for Plan Administrators

In April, the Supreme Court ruled on the vitality of the deferential standard of review that ERISA plan administrators have in the determination of benefit claims.

Conkright v. Frommert involved a case concerning the proper interpretation of a provision in the Xerox Pension Plan that the plan administrator contended allowed it to impute earnings to earlier lump-sum distributions in calculating offsets for employees who returned to employment and earned additional benefits after receiving the distributions. The district court initially affirmed the plan administrator's interpretation, but the Second Circuit Court of Appeals reversed, holding that the interpretation was unreasonable. On remand, the plan administrator presented a new interpretation of the provision to the district court, but the court gave it no deference and rejected it, adopting the employees' proposed approach instead. The Second Circuit affirmed the district court's refusal to review the plan administrator's new approach under a deferential standard, because the plan administrator had already abused its discretion in interpretation the provision in the first instance, according to the court.

The Supreme Court, however, rejected the Second Circuit's ruling, holding that the robust standard of deference enunciated in Firestone Tire & Rubber Co. v. Bruch and Metropolitan Life Ins. Co. v. Glenn does not disappear merely because a plan administrator mistakenly interprets a plan provision. The Court held the district court should have reviewed the plan administrator's second interpretation of the plan provision at issue under a deferential standard of review, rather than substituting its own judgment for that of the plan administrator.

Note: The decision is significant for plan administrators, as it supports the continued viability and vitality of the deferential standard of review, in the absence of bad faith on the part of the plan administrator.