Trap for the Unwary – Be Careful with Amendments to Your Nonqualified Plans

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PRACTICES Employee Benefits and Executive Compensation

While so-called "top hat plans" for executives are exempt from many of ERISA's onerous requirements (as we previously discussed here), be wary of your plan's amendment language. A recent decision from the Eleventh Circuit U.S. Court of Appeals ("***Eleventh Circuit***") illustrates that top hat plan amendment and termination language could trigger a breach of contract claim.

In *Hoak v. Ledford*, top hat plan participants (the "***Participants***") filed a class action complaint for breach of contract against NCR Corporation (the "***Plan Sponsor***" and "***Plan Administrator***"), the Compensation and Human Resources Committee, and certain officers of the Plan Sponsor, alleging that the defendants adversely affected their accrued benefits earned under several top hat plans by amending their forms of benefit distributions.

The Participants had all accrued benefits under one of the five top hat plans maintained by the Plan Sponsor (the "***Plans***"), each of which provided fixed monthly annuities for life. Under the terms of each Plan, the Plan Sponsor had the power to amend or terminate such Plan, "provided . . . that (a) no such action shall adversely affect any Participant's . . . accrued benefits prior to such action under the Plan . . .".

The Plan Sponsor decided to terminate the Plans. After hiring consultants to review all distribution options, the Plan Sponsor decided to convert each Participant's life annuity to a lump-sum distribution that was actuarially equivalent to the annuity benefit. The Participants sued in the U.S. District Court for the Northern District of Georgia ("***District Court***"), which found, on summary judgment, that the accrued benefits under the Plans were adversely affected by this lump-sum conversion.

The Plan Administrator appealed the judgment to the Eleventh Circuit, contending that it had reserved the discretion under each Plan to interpret its terms, particularly the phrase "no such action *shall adversely affect* any . . . benefits." However, the Eleventh Circuit disagreed with this argument, finding that the Plans "did not expressly permit NCR to pay the [P]articipants its chosen actuarially equivalent lump sums (with or without a discount rate) upon termination as an alternative to their promised life annuities." As a result, the Plan Administrator did not have the discretion to interpret what the Eleventh Circuit determined was an unambiguous provision of the Plans. The Eleventh Circuit thus affirmed the District Court's order to pay the Participants the difference between their lump sum distributions and the cost of replacement annuities.

An important takeaway for an employer-sponsor of a top hat plan is that the plan's language pertaining to plan amendments, or termination of the plan itself, needs to be carefully drafted to preserve the employer's discretion, otherwise the employer could be contractually limited in its rights to take future actions.

The Eleventh Circuit opinion is available here.