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Subject: **Court Holds That Employer has the Right to Terminate Top-Hat Plan, Including Split-Dollar Life Insurance Policy, Despite Promises Made to Executive**

Major References: [*Panecasio v. Unisource Worldwide, F3d \(2d Cir., July 7, 2008\)*](#)

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The Second Circuit Court of Appeals, in Panecasio v. Unisource Worldwide, F.3d. (2d. Cir., July 7, 2008), recently held that an employer was allowed to terminate its top-hat deferred compensation plan and split-dollar life insurance arrangement for an executive six months before he reached retirement. The executive alleged that, due to certain promises made to him, the company had guaranteed his entitlement to the retirement and life insurance benefits at age 65.

The employer (Unisource Worldwide, Inc., a previous subsidiary of IKON Office Solutions, Inc.) created a contributory, defined benefit top-hat plan with a split-dollar life insurance benefit starting in 1991. Under the plan, participants were allowed to defer a portion of their income until retirement and were potentially eligible to receive certain retirement and life insurance benefits. The life insurance benefit included death benefit coverage until retirement and a transfer of a split-dollar policy to the participant at age 65. In terms of retirement benefits, the employees had certain options under the plan. The executive in this law suit chose an option which would have provided him with a \$15,000 per year annuity for 10 years starting at age 65 and a life insurance policy with a \$95,000 cash value and a paid-up death benefit of \$375,000. Under this plan, however, if the plan is terminated or the participant does not reach retirement age, then the participant only receives back his actual cumulative contributions at 6% interest.

The executive who brought the suit worked for the employer from 1971 until 1994 when he retired at age 57 pursuant to an early retirement package offered by the employer. As part of the early retirement package, the executive received 65% vesting in the deferred compensation plan. This meant that his 10-year payment at age 65 would be \$9,750 and the life insurance policy would allow for a post-age 65 cash value of \$61,750 and a death benefit of \$243,750.

The executive received a number of written materials as part of this early retirement package. In those materials was a disclaimer that referenced the fact that the documents were only summaries of the early retirement package and that more detailed information was available from plan documents and insurance contracts. It then stated in language that was both bolded and highlighted, “In case of any dispute, the official legal documents or contracts will govern over this brochure.” However, the brochure specifically reserved the right to change medical and dental benefits but did not include a similar provision specifically referencing the deferred compensation plan.

The deferred compensation plan itself had a termination provision which was somewhat unusual in its wording. It stated that the board of directors of IKON had the right to terminate the plan at any time if it “determines that proposed or pending tax law changes or other events cause, or are likely in the future to cause, the Plan to have an adverse financial impact upon [IKON].” In 2000, the IKON board of directors decided to terminate the plans on the grounds of unfavorable interest rates and declining participation. It appears from the court’s opinion that the plan was designed to assume a level of contribution by a number of executives which did not materialize. As a consequence, the cost of the plan has exceeded the contributions by about \$1 million. The plan was terminated with respect to the executive (and the other executives) and he was refunded his contributions and interest in a lump sum amount of \$75,419, which, under the terms of the plan, was the only benefit he was entitled to. Had the plan been terminated six months later it appears that he would have been entitled to his vested retirement and life insurance benefits pursuant to the provisions of the early retirement package.

The executive appealed his denial of benefits, which was denied on the basis that the vesting in the early retirement package did not supersede the termination provisions found in the deferred compensation plan. The lower court upheld this position, deferring in large part to the committee’s decision as not being “arbitrary and capricious” under ERISA review standards and therefore, entitled to deference by the court. The Court of Appeals for the Second Circuit upheld the position of the lower court.

The Court of Appeals sustained the lower court’s ruling on several grounds. First, it agreed with the lower court that the decision of the benefits committee on appeal was not arbitrary and capricious and therefore that decision should be upheld. In addition, it concluded that the executive’s reliance on the early retirement package provision was “unreasonable” and would not support estoppel of the company’s decision to terminate the plan. At trial the executive admitted that he had read the terms of both the retirement plan and the early retirement package and was aware of the disclaimer and understood these items. He also did not offer any evidence of any direct oral misrepresentation to support his reading of the documents that he was 65% vested in the top-hat benefits in any event.

In this regard, the court’s decision is somewhat striking because similar disclaimer language has often been ignored by courts (including courts in the Second Circuit) when that language is contained in a summary plan description of a pension plan. Courts have often allowed employee/plaintiffs to prevail in situations where misleading language (to the employee’s benefit) is contained in a summary plan description but correct language is contained in the plan document, even though the summary plan description says that the plan document controls. Here, however, the court was not persuaded that the summary should control. The court reached this conclusion, despite its discomfort with the fact that the

earlier retirement package summary had specifically pointed out the right to change medical and dental benefits and did not have a similar specification with respect to the top-hat benefits.

In addition to his ERISA claims, the executive brought claims under the Age Discrimination in Employment Act (ADEA) and under state law. The ADEA claims were dismissed because they had not been timely brought. The executive waited seven years before filing a complaint with the EEOC, alleging unlawful employment practices. The court found that the executive did not make a sufficient case for tolling the statute of limitations. (He argued that he did not bring the case earlier because the misrepresentations had made him believe he would be paid the benefit at age 65).

The court also held that the state law claims were preempted. The executive sought to apply state law even though ERISA states that it preempts state law with respect to issues related to a pension plan (which includes top-hat plans). Because top-hat plans are not subject to the substantive rules (including the fiduciary responsibility rules) of ERISA, the executive argued that state law with respect to those types of claims should not be preempted. Although this argument appears to have been settled many years ago though a series of cases, the court here re-analyzed those cases and again held that all state law claims were preempted because a top-hat plan is, nevertheless, a pension plan under ERISA.

The case is interesting in both its analysis and result. Often courts bend over backwards to favor the individual who is threatened with a loss of benefit, especially when that benefit is sought to be eliminated a short period before the executive would have been entitled to it (in this case, six months before retirement). It is also interesting that the court placed so much reliance on the disclaimer when in other circumstances the courts have essentially ignored similar disclaimers. One notable difference is that here the plaintiff was an executive, whereas in the typical qualified plan case the individual is not highly compensated. In addition, the nature of the plan, its termination provisions and the court's analysis are unusual. Finally, the plan did not contain an absolute right of termination -- only a conditional right (due to interest rates, changes in the law and other similar factors). Nevertheless, the court was not bothered by the conditionality of that right. It simply applied the "arbitrary and capricious" standard to uphold the termination right.

Any AALU member who wishes to obtain a copy of *Paneccasio v. Unisource Worldwide* may do so through the following means: (1) use hyperlink above next to "Major References," (2) log onto the AALU website at www.aalu.org and enter the *Member Portal* and select *Current Washington Report* for linkage to source material or (3) email Erik Ruselowski at ruselowski@aalu.org and include a reference to this *Washington Report*.

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