

Amending Tennessee Governmental Pension Plans: Current State of the Law

Presented by:

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Plan Modifications Under ERISA

- ▶ A plan sponsor is generally prohibited from amending a plan if the amendment would reduce a participant's accrued benefit, but may amend a plan to decrease the rate of future accruals. ERISA § 204; Code § 411(d)(6).
- ▶ “Accrued Benefit” in a defined benefit plan is the “accrued benefit determined under the plan and . . . expressed in the form of an annual benefit commencing at normal retirement age.” ERISA § 3(23).
- ▶ A benefit is vested or “nonforfeitable” when a participant or beneficiary obtains an unconditional, legally enforceable right to an immediate or deferred benefit under a pension plan. ERISA § 3(19).

Plan Modifications Under *Blackwell*

- ▶ *Blackwell v. Quarterly County Court of Shelby County* (1981): TN Supreme Court established rule limiting power of governmental bodies in TN to change their retirement systems
- ▶ Court asserts that “public policy demands that there be a right on the part of the public employer to make reasonable modifications in an existing plan if necessary to create or safeguard actuarial stability, provided that no then accrued or vested rights of members or beneficiaries are thereby impaired”
- ▶ The *Blackwell* rule: reasonable modifications to governmental pension plans permitted “when necessary to protect or enhance the actuarial soundness of the plan, provided that no such modification can adversely affect an employee who has complied with all conditions necessary to be eligible for a retirement allowance”

Interpretation of *Blackwell*

▶ Increasing Employee contributions

- ▶ Prohibits requiring vested employees who have not previously contributed to the plan to begin contributing. Att’y Gen. 05-058 (April 2005).
- ▶ Dicta in *Blackwell* provides that an increase in the amount of employee contributions “could probably be considered favorable to employees . . .”

▶ Modifying creditable service requirements

- ▶ Plan cannot be amended to eliminate a provision allowing an employee to count education leave as creditable service for vested participants. Att’y Gen. 97-012 (February 1997).

Interpretation of *Blackwell* (Cont'd)

▶ Modifying benefit base

- ▶ Adverse changes in a benefit base cannot be applied to employees who, as of the effective date of the amendment, have the minimum requisite years of creditable service under the plan even though they cannot actually begin drawing benefits until they reach retirement age. *Roberts v. TCRS*, 622 S.W.2d 544 (Tenn. 1981); *Felts v. TCRS* S.W.2d 371 (Tenn. 1983) .

▶ Changes to retiree health insurance

- ▶ Retiree health insurance is a welfare benefit rather than a pension benefit and may be modified or terminated. *Davis v. Wilson County*, 70 S.W.3d (Tenn. 2002).

Interpretation of *Blackwell* (Cont'd)

- ▶ Accepting modification
 - ▶ Employee or public official may consent to adverse modification of pension by their acceptance of re-election, re-appointment, promotion, or change in classification. Att'y Gen. 05-163 (October 2005); Att'y Gen. 05-152 (October 2005); Att'y Gen. 04-114 (July 2005).
- ▶ Changes to administrative procedures
 - ▶ Amendment changing a provision that a participant's divorce does not automatically cancel a beneficiary designation is merely an administrative issue, not a right protected by *Blackwell*. *Mathews v. Burkeens*, 763 S.W.2d 739 (Tenn. 1988).
- ▶ Changes to treatment of accumulated sick leave
 - ▶ Government's practice of cashing out sick leave benefits upon retirement involves inchoate rights that do not vest. Employer was free to change way and manner of compensating employees for unused sick leave without implicating *Blackwell*. *Carson v. City of LaFollette*, 878 S.W.2d 953 (Tenn. Ct. App. 1994).

Interpretation of *Blackwell* (Cont'd)

- ▶ Changing disability benefit
 - ▶ Ordinance reducing amount of disability pension benefits may not be applied to reduce the benefits of an employee who complied with all conditions precedent to receipt of full disability pension before effective date of ordinance. *Neblette v. City of Chattanooga Fireman's & Policeman's Ins. & Pension Fund Bd.*, No. 03A01-9511-CH-00418, 1196 WL 269469 (Tenn. Ct. App. May 22, 1996).
 - ▶ Welfare benefits may be modified or terminated at any time unless the employee meets the burden of establishing that the employer expressly provided that the benefits were intended to vest or were not to be terminated. “The law is clear that there is no legal requirement on the part of the governmental entity to provide a welfare benefit plan to its employees and if it chooses to do so, the plan may be modified or terminated at any time.” *Davis v. Wilson Cty.*, 70 S.W.3d 724 (Tenn. 2002).

TN Attorney General Opinion

- ▶ Opinion 15-18 (March 12, 2015)
- ▶ Recognizes that *Blackwell* not only protects benefits that have accrued as of the date of a plan modification, but also a vested employee's right to continue accruing benefits in accordance with the terms of the plan before modification
 - ▶ “Vested” means that an employee “must have met all eligibility requirements to receive a retirement benefit in the future, but the employee need not have attained the minimum retirement age or the right to receive pension benefits”
- ▶ Points out that *Blackwell* and its progeny restrict modification despite language in the plan authorizing the amendment or repeal of the terms of the plan

TN Attorney General Opinion (Cont'd)

- ▶ Concludes that while a general reservation of right to amend a plan, without more explanation, may be ineffective, a public employer may amend a retirement plan to reduce future benefit accruals of vested participants so long as it adequately reserves the right
- ▶ Plan must be sufficiently specific and clear to notify members not only that the public employer may amend the plan from time to time, but that the employer may alter vested members' rights under the plan, including the right to accrue future benefits
- ▶ Sample language from TCRS Hybrid Plan:
 - ▶ plan reserves the right to “freeze, suspend, or modify benefits, employee and employer contributions, plan terms and design of the hybrid plan on a prospective basis”
 - ▶ “nothing under state law may confer to participants in the hybrid plan an implied right to future retirement benefit arrangements and such participants may not assert the indefinite continuation of retirement formulas, contribution rates, eligibility ages, or any other provision of the plan”

Duncan v. Muzyn, TVARS, & TVA

- ▶ August 12, 2016 (6th Cir. Ct. of Appeals)
- ▶ TVARS amended to cap or eliminate COLAs for 2010-2013 and to increase the eligibility age for COLA adjustments
- ▶ Court held that the COLA is not a vested benefit
- ▶ Amendment did not deprive participants of a protected property right because the Plan did not “unmistakably intend to prevent itself from reducing COLAs”

Frazier v. City of Chattanooga Fire and Police Pension Fund

- ▶ November 3, 2016 (6th Cir. Ct. of Appeals)
- ▶ Pension codified in City Code
- ▶ In 2000 COLA fixed at 3%
- ▶ In 2014 COLA variable as follows:
 - ▶ When plan < 80% funded, 1½ % increase w/those receiving higher pensions getting lower increase (1% minimum)
 - ▶ When plan at least 80% funded, tied to CPI w/ 3% maximum
- ▶ Retirees sued asserting violation of the US Constitution Contracts Clause

Chattanooga Pension Case (Cont'd)

- ▶ Court held retirees do not have a contractual right to the fixed 3% COLA, because the City Code does not bind the plan to the fixed COLA
- ▶ A statute merely expresses current government policy and future legislatures are free to change that policy
- ▶ Absent clear indication that the legislature intends to bind itself contractually, a statute does not create a contractual relationship
- ▶ Retirees have the burden of showing that the City Code contains an unmistakable promise precluding the City from exercising its sovereign power to reduce the COLA

Chattanooga Pension Case (Cont'd)

- ▶ City Code does not unmistakably bind the plan to the fixed 3% COLA
- ▶ City may amend the plan “provided that such amendment shall in no way decrease any vested financial benefits accrued by any participant or beneficiary”
- ▶ City expresses intent to be bound only to vested, accrued financial benefit

Chattanooga Pension Case (Cont'd)

- ▶ COLA is not a “vested benefit” because the City did not include it in the plan’s vesting provision
 - ▶ Plan provision that COLA “shall be increased” by 3% does not mean COLA is vested
 - ▶ “shall” only imposes a duty on government officials to apply the COLA each year until the legislature amends it
- ▶ COLA is not an “accrued financial benefit” because it is not an “enforceable right” until January 1 of each year
 - ▶ Future increases pursuant to fixed COLA had not “accrued” as of the date of the 2014 amendment
- ▶ No unmistakable evidence that the 3% fixed COLA is a vested or accrued benefit

Chattanooga Rule Applied: Anytown Pension Plan

- ▶ Anytown's Charter gives Pension Board power to amend the Plan
- ▶ Plan provides: “no amendment shall reduce any Participant's or Beneficiary's benefit that is vested and accrued under the Plan as of the date such amendment is adopted . . .”
- ▶ COLA provision: Commencing 1 full calendar year after retirement, benefit shall be increased annually by 3%
- ▶ Plan's vesting provisions do not mention the COLA
- ▶ COLA does not accrue until January 1 each year

Chattanooga Rule Applied: Nowheresville Pension Plan

- ▶ Plan provides “employer may... amend the plan at any time... in accordance with Tennessee law applicable to governmental plans”
- ▶ COLA Provision: each January 1, adjustment measured by CPI, up to 3%
- ▶ Plan’s vesting provisions do not mention COLA
- ▶ COLA does not accrue until January 1 each year

Chattanooga Rule Applied: ABC Electric Company Pension Plan

- ▶ Charter gives ABC power to amend the Plan at any time
- ▶ Plan provides “no amendment, unless it is necessary to meet the requirements of any state or federal law, shall operate to deprive any Participants of any benefits, to the extent they are funded.”
- ▶ COLA provision: commencing 12 months after retirement, benefit shall be adjusted annually by 3%, plus an additional amount (tied to CPI) for those over age 62
- ▶ Plan’s vesting provisions do not mention the COLA
- ▶ COLA does not accrue until January 1 each year

What Changes are Permitted?

- ▶ Detrimental modifications:
 - ▶ To benefits of current, non-vested employees if reasonable and necessary to protect or enhance actuarial soundness of the plan
 - ▶ To benefits of vested employees with their consent
 - ▶ That affect only new hires
 - ▶ Where a promotion, different appointment, or change in classification is conditioned on such modifications and the employee consents
 - ▶ To health and welfare plans
 - ▶ To administrative or ancillary features

What Changes are Arguably Permitted?

- ▶ Detrimental modifications:
 - ▶ To disability benefit
 - ▶ To death benefit
 - ▶ If plan document reserves right to amend prospectively
 - ▶ To COLAs
 - ▶ To employee contributions
 - ▶ To form of distribution
 - ▶ To discount rate and actuarial assumptions
- ▶ Plan termination (or hard freeze)

Questions Remaining

- ▶ Would a Tennessee court reach a different conclusion on facts similar to the Chattanooga case based on state law?
 - ▶ Chattanooga case decided on US constitutional contract law grounds
 - ▶ Looks at plan's amendment provision and concludes that City expressed an intent to be bound only to "vested, accrued financial benefits" and could otherwise amend plan to change plan provisions that are not vested or accrued
 - ▶ *Blackwell* decided as a matter of state public policy
 - ▶ Concludes that governmental employer may not make modifications to plan that would adversely affect benefits of a vested employee
 - ▶ Attorney General interpretation suggests amendment to future benefit accruals would be permissible if plan is sufficiently clear and specific that employer may amend vested employee's rights, including right to accrue future benefits
- ▶ Do the terms "vested" and "accrued" mean something different under state and federal law?

Additional Information on the Firm

Kennerly Montgomery is a general practice law firm that has provided legal advice to clients for 100 years. KM attorneys practice in a variety of areas, representing private employers, non-profits, and municipal clients, including local governments, agencies and public utilities.

Bill Mason, Kathy Aslinger, and Ashley Trotto practice extensively in employment and employee benefits law, which includes advising employers on individual employee issues, employment contracts, employee handbooks, as well as design, documentation, administration, audit, litigation, termination and qualification of employee health and welfare and pension plans for public, tax-exempt and private employers. They represent clients before various agencies regulating employment issues and employee benefits.

A Little About Your Presenters

Bill Mason received his law degree from Harvard Law School in 1974, and has been practicing more than 40 years, most of that time in employment and employee benefits for employers. He worked for the Tennessee Valley Authority from 1974 – 1986, Wagner Myers & Sanger PC, from 1986 – 1988, and William E. Mason PC from 1988 – 2009. Bill joined Kennerly Montgomery in 2009. He serves on the Board of Directors for the Legacy Park Foundation and the Education Subcommittee for the United Way of Greater Knoxville. He is the past Chair of the Hillcrest Healthcare Board of Directors. In 2016, the US Treasury Department appointed him as the IRS Taxpayer Advocacy Panel (TAP) representative for Tennessee.

As a leader of Kennerly Montgomery's employee benefits practice, Kathy Aslinger focuses on advising fiduciaries for the benefit of participants, assisting both private and governmental clients in the design, implementation and maintenance of their employee benefit plans, including 401(k), pension, cafeteria, and health plans. She commonly assists clients in maneuvering through the complex world of audits, fiduciary liability issues, DOL and IRS compliance, HIPAA, COBRA, ERISA and state law obligations, as well as Affordable Care Act compliance. Kathy has been practicing law for over 17 years and has been with Kennerly Montgomery since January 2010. In addition, Kathy serves on the Board of Directors for Uplands Village, a continuing care retirement community in Pleasant Hill, Tennessee.

Ashley Trotto joined Kennerly Montgomery as an associate attorney in the Firm's employment law and employee benefits practice in 2013. Ashley concentrates on the Affordable Care Act and health and welfare plan compliance. She also regularly assists clients in navigating through the FLSA, HIPAA, COBRA, FMLA, ADA and other employment-related legislation. Ashley serves on the Board of Directors for the Smoky Mountain Animal Care Foundation and is also a member of the East Tennessee Benefits and Compensation Association, serves on the Hunger and Poverty Relief Committee of the Knoxville Bar Association and is a member of the United Way Health and Basic Needs Investment Committee. She's also the energy behind the Firm's on-going kindergarten book project at Christenberry Elementary.

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