

1 UNITED STATES COURT OF APPEALS

2
3 FOR THE SECOND CIRCUIT

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6
7 August Term 2008

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9 (Argued: March 20, 2009 Decided: October 19, 2009)

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11 Docket Nos. 08-0459-cv (L); 08-0538-cv (XAP)

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15 MICHAEL LONECKE, RAYMOND DUFFY,
16 ANNE NELSON, ROBERT S. FASH, AND
17 CRAIG A. HARRIS, INDIVIDUALLY AND ON
18 BEHALF OF ALL THOSE SIMILARLY SITUATED,

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20 *Plaintiffs-Appellees-Cross-Appellants,*

21
22 WILLIAM WOODWARD, INDIVIDUALLY AND
23 ON BEHALF OF ALL THOSE SIMILARLY SITUATED,

24
25 *Plaintiff-Appellee,*

26
27 -v.-

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29 CITIGROUP PENSION PLAN, PLANS ADMINISTRATION
30 COMMITTEE OF CITIGROUP, INC., CITIGROUP, INC.,

31
32 *Defendants-Appellants-Cross-Appellees.*

1 Before: JACOBS, *Chief Judge*, WESLEY, *Circuit Judge*, and
2 CROTTY,* *District Judge*.
3

4 Appeal from an order of the United States District
5 Court for the Southern District of New York (Scheidlin,
6 *J.*), entered on December 11, 2006, granting partial summary
7 judgment to Plaintiffs.
8

9 REVERSED.
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13 EDGAR PAUK, Law Office of Edgar Pauk, Esq.,
14 Brooklyn, New York, and Brad Nelson Friedman,
15 Milberg LLP, New York, New York, for
16 *Plaintiffs-Appellees-Cross-Appellants*.
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18 DEREK W. LOESER, Keller Rohrback LLP, Seattle,
19 Washington, for *Plaintiff-Appellee*.
20

21 MYRON D. RUMELD, Proskauer Rose LLP, New York, New
22 York; LEWIS R. CLAYTON, Paul, Weiss, Rifkind,
23 Wharton & Garrison, LLP, New York, New York,
24 for *Defendants-Appellants-Cross-Appellees*.
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28 WESLEY, *Circuit Judge*:

29 Plaintiffs are five present or former employees of
30 either Smith Barney or Citibank, N.A., both of which are
31 divisions of Citigroup, Inc. ("Citigroup"). Plaintiffs, and
32 the class they represent, allege that the Citibuilder Cash

* The Honorable Paul A. Crotty, United States District
Judge for the Southern District of New York, sitting by
designation.

1 Balance Plan ("Plan") violates the Employee Retirement
2 Income Security Act of 1974 ("ERISA"), as amended, 29 U.S.C.
3 § 1001 et seq. Plaintiffs seek injunctive and declaratory
4 relief as well as monetary damages.

5 By order dated December 11, 2006, the United States
6 District Court for the Southern District of New York
7 (Scheidlin, J.) granted partial summary judgment to
8 Plaintiffs on various grounds, including: first, that the
9 Plan violated ERISA's minimum benefit accrual rules through
10 its use of the "fractional rule"; and second, that Citigroup
11 violated ERISA's § 204(h) notice requirement. 29 U.S.C. §
12 1054(h).¹ Citigroup challenges those two conclusions.
13 Plaintiffs cross-appeal, raising a number of issues. On
14 appeal, both parties agree that the district court erred in
15 concluding that the "fractional rule" can never properly be

¹ The district court also concluded that the structure of the Plan violated ERISA's age discrimination rules. However, subsequent to the district court's opinion in this case, a panel of this court held that "cash balance . . . plans do not by definition violate ERISA's prohibition against age-based reductions in the rate of benefit accrual." *Hirt v. Equitable Ret. Plan for Employees, Managers & Agents*, 533 F.3d 102, 110 (2d Cir. 2008). The age discrimination count, therefore, is not part of this appeal.

1 applied to cash balance plans, such as Citigroup's Plan.
2 Because we find that Citigroup's Plan does not violate
3 ERISA's minimum benefit accrual rules, and that Citigroup
4 did not violate ERISA's § 204(h) notice requirements, we
5 reverse.

6 **I. BACKGROUND**

7 **A. ERISA Benefit Plans Generally**

8 ERISA recognizes two basic types of retirement plans:
9 defined contribution plans and defined benefit plans. *Hirt*
10 *v. Equitable Ret. Plan for Employees, Managers & Agents*, 533
11 F.3d 102, 104 (2d Cir. 2008). Defined contribution plans,
12 also known as individual account plans, "guarantee only that
13 the employer will contribute [a certain amount] to the
14 [employee's retirement] account," without providing any
15 guarantee as to that account's value upon the employee's
16 retirement. *Id.* at 105; see also 29 U.S.C. § 1002(34). A
17 defined contribution plan is a "pension plan which provides
18 for an individual account for each participant and for
19 benefits based solely upon the amount contributed to the
20 participant's account, and any income, expenses, gains and

1 losses." 29 U.S.C. § 1002(34).² Both the employee and the
2 employer may contribute to a defined contribution plan, but
3 the employer's contribution is fixed. *Hughes Aircraft Co.*
4 *v. Jacobson*, 525 U.S. 432, 439 (1999).

5 Defined benefit plans "generally guarantee [employees]
6 a specific benefit [upon retirement] without regard to how
7 the market performs." *Hirt*, 533 F.3d at 105; see also 29
8 U.S.C. § 1002(35). In contrast to a defined contribution
9 plan, a defined benefit plan "consists of a general pool of
10 assets rather than individual dedicated accounts." *Hughes*
11 *Aircraft Co.*, 525 U.S. at 439. The pool of assets "may be
12 funded by employer or employee contributions, or a
13 combination of both." *Id.* In a defined benefit plan, "no
14 plan member has a claim to any particular asset that
15 composes a part of the plan's general asset pool." *Id.* at
16 440. Rather, members have a right to a defined level of
17 benefits, known as accrued benefits. *Id.* In a defined
18 benefit plan, an accrued benefit is "expressed in the form
19 of an annual benefit commencing at normal retirement age."

² A 401(k) plan is a common defined contribution plan.
See *Hirt*, 533 F.3d at 104; see also 29 U.S.C. § 1002(34).

1 29 U.S.C. § 1002(23)(A). Whereas, in a defined contribution
2 plan, the accrued benefit is understood as "the balance of
3 the individual's account." 29 U.S.C. § 1002(23)(B).

4 Defined contribution and defined benefit plans
5 primarily "differ in who bears the risk of investment
6 performance." *Hirt*, 533 F.3d at 105. In a defined
7 contribution plan, the employee bears the risks, while in a
8 defined benefit plan, "the employer typically bears the
9 entire investment risk." *Hughes Aircraft Co.*, 525 U.S. at
10 439. In a defined benefit plan, the employer is obligated
11 to "cover any underfunding as the result of a shortfall that
12 may occur from the plan's investments." *Id.* And, if a
13 defined benefit plan is overfunded, the employer "may reduce
14 or suspend [its] contributions." *Id.* at 440.

15 Within the context of these two types of retirement
16 plans, employers have developed a relatively new kind of
17 plan called a "cash balance plan." *Hirt*, 533 F.3d at 105.
18 The cash balance plan is "intended to combine attributes of
19 both defined contribution and defined benefit plans." *Id.*
20 "[C]ash balance plans are often described as 'hybrid': they
21 create a benefit structure that simulates that of defined

1 contribution plans, but employers do not deposit funds in
2 actual individual accounts, and employers, not employees,
3 bear the market risks." *Id.* Cash balance plans are
4 considered defined benefit plans under ERISA because the
5 accounts are hypothetical in nature and the employee
6 receives a specified lump-sum payout upon retirement. *Esden*
7 *v. Bank of Boston*, 229 F.3d 154, 158 (2d Cir. 2000); see
8 also 29 U.S.C. § 1002(35). As a result of this
9 classification, the term "accrued benefit" in a cash balance
10 plan is "expressed in the form of an annual benefit
11 commencing at normal retirement age." *Esden*, 229 F.3d at
12 163 (quoting 29 U.S.C. § 1002(23)(A)).³

13 When an employer establishes a cash balance plan, an
14 account is created in the name of each participant to keep
15 track of his or her accrued benefits. *Bilello v. JPMorgan*

³ In 2006, Congress enacted the Pension Protection Act ("PPA"), which amended ERISA to allow specifically for cash balance defined benefit plans. Pub. L. No. 109-280, § 701(a)(1), 120 Stat. 780, 981 (2006). The amendment applies to periods commencing on or after June 29, 2005. *Id.*; § 701(e)(1), 120 Stat. at 991. Because Plaintiffs' challenge to the Citibuilder Cash Balance Plan concerns a period prior to the PPA's effective date, the terms of the PPA are not implicated by this appeal. In any event, as we have held, "[e]ven prior to the PPA, cash balance plans could survive scrutiny under ERISA." *Hirt*, 533 F.3d at 104.

1 *Chase Ret. Plan*, – F. Supp. 2d –, No. 07-cv-7379 (DLC), 2009
2 WL 2461005, at *1 (S.D.N.Y. Aug. 12, 2009). In a cash
3 balance plan, the account contains “pay credits,” which
4 “represent[] a percentage of the participant’s salary that
5 is periodically deposited into the account, as well as
6 ‘interest credits,’ which apply a common interest rate to
7 the account balances.” *Id.* Pay credits only accumulate
8 until the termination of the participant’s employment, but
9 interest credits continue to accrue until the benefits are
10 distributed. *Id.* In a cash balance plan, the employer may
11 offer the employee the option of a lump sum payout instead
12 of an annuity; however, “any such payout must be worth at
13 least as much, in present terms, as the annuity payable at
14 normal retirement age.” *Id.*

15 Proponents of cash balance pension plans assert that
16 this “hybrid” structure is beneficial for employees because
17 it is easier for them to understand, it allows for greater
18 portability, it establishes a system whereby benefits accrue
19 more evenly over an employee’s career, and it is
20 “therefore[] better suited to the increased job-mobility of
21 contemporary labor markets.” *Esdan*, 229 F.3d at 158 n.5.

1 Advocates of cash balance plans also maintain that they
2 benefit employers. They suggest that "because employees
3 better appreciate the value of their pension rights, the
4 employer's fringe benefit dollar has greater impact." *Id.*
5 They also argue that a cash balance plan "retains the
6 funding advantages of a defined benefit plan" for the
7 employer. *Id.* Specifically, "actual contributions are made
8 to a single trust fund, based on actuarial assumptions;
9 therefore . . . the employer retains funding flexibility as
10 long as the solvency of the plan is maintained;" and
11 investment returns that exceed "the promised interest
12 credits (as well as forfeitures of the non-vested benefits
13 of any terminated participants)" are retained by the
14 employer. *Id.* Almost one-third of all single-employer
15 defined benefit plan participants – approximately ten
16 million workers – are covered by cash balance plans, or
17 other similar hybrid plans.

18 **B. The Citigroup Plan**
19

20 In 1998, Citicorp merged with Travelers Corporation.
21 Authority to amend Citibank's pension plan was vested in the
22 plan sponsor, Citigroup, by action of its Board of

1 Directors. In 1999, at a meeting of the Board of Directors,
2 Citigroup converted its traditional, final pay pension
3 formula into a cash balance plan. The Citigroup Board
4 adopted a series of resolutions in October of 1999
5 incorporating the cash balance design into the Plan. The
6 conversion had an effective date of January 1, 2000.

7 In May of 2001, the provisions of the newly adopted
8 cash balance plan were set forth in Plan Article 4.1. Under
9 the Plan, Citigroup created a hypothetical account for each
10 participating employee, and then "credited" each account
11 with two kinds of "deposits" - Benefit Credits and Interest
12 Credits. Benefit Credits were awarded to participants as a
13 percentage of that year's total compensation. Under the
14 Plan's formula, Benefit Credits increased with age and years
15 of service, ranging from two percent for participants under
16 age twenty-five in their first ten years of service, to
17 seven percent for participants fifty years or older with
18 fifteen or more years of service. Interest credited to the
19 account was awarded based on an extrinsic index rate - the
20 thirty-year Treasury rate. At retirement, participants
21 would be entitled to a lump sum payout based on the

1 accumulated value of their accounts, or to an actuarially
2 equivalent pension.

3 Although the provisions of the amendments were not set
4 forth in an executed Citibuilder Retirement Plan document
5 until May of 2001, in the months leading up to the effective
6 date Citigroup sent out a number of brochures and pamphlets
7 concerning the changes to the structure of the benefit plan.
8 Pursuant to ERISA § 204(h), official notice of the amendment
9 was given to all Plan participants in a letter from Tim
10 Peach, Director of Retirement Benefits, dated December 9,
11 1999. The letter was entitled: "The Citigroup Pension Plan
12 Notice of Significant Reduction in Benefit Accruals for
13 Certain Employees of Citigroup Inc. and its Subsidiaries"
14 (the "1999 Notice").

15 The 1999 Notice contained a general summary of how the
16 new cash balance plan would work, as well as a table listing
17 the percentages of salaries credited to accounts annually,
18 as determined by an employee's age and years of service.
19 The cover letter referenced ERISA § 204(h) and explained
20 that, due to the forthcoming amendments to the pension plan,
21 it was "likely that some employees would see some level of

1 reduction in total accumulations in the future." The
2 documentation accompanying the letter, distributed to each
3 affected employee, also outlined the mechanisms of a cash
4 balance plan. It explained that under the Plan as amended,
5 the "company credits a percentage of your total compensation
6 each year to a hypothetical account. That percentage
7 generally increases with your age and service." The 1999
8 Notice also explained that "the hypothetical account earns
9 interest credits at a rate based on 30-year Treasury bonds."
10 The 1999 Notice did not, however, indicate the formula that
11 the Plan would apply in order to achieve compliance with
12 statutory accrual principles.

13 The Plan was again amended, effective January 1, 2002.
14 This amendment incorporated the same cash balance regime
15 adopted in 2000, but recalibrated the range of Benefit
16 Credits allotted annually to employees' accounts. Pursuant
17 to this amendment, Benefit Credits ranged from one and one-
18 half percent for participants under age twenty-nine in their
19 first five years of service, to six percent for those fifty-
20 five or older with fifteen or more years of service.
21 Citigroup employed a notification process similar to the

1 process it utilized in 1999. Pursuant to ERISA § 204(h), an
2 information package dated December 2001 was sent to Plan
3 participants informing them of the amendment. As with the
4 1999 Notice, there was no mention of the means by which the
5 Plan would ensure compliance with ERISA's accrual
6 requirements.

7 **C. The Minimum Benefit Accrual Tests**

8 Cash balance plans, such as the Citibuilder Plan, are
9 defined benefit plans within the meaning of ERISA because
10 they guarantee a prescribed level of retirement benefits.
11 *Esdén*, 229 F.3d at 158; see also 29 U.S.C. § 1002(35). All
12 defined benefit plans must comply with ERISA's minimum
13 benefit accrual rules, which are primarily designed to
14 minimize "backloading." *Langman v. Laub*, 328 F.3d 68, 71
15 (2d Cir. 2003); H.R. Rep. No. 93-807 (1974), reprinted in
16 1974 U.S.C.C.A.N. 4639, 4688. Backloading occurs when a
17 plan awards a covered employee disproportionately higher
18 benefit accruals for later years of service. *Langman*, 328
19 F.3d at 71. Thus, while ERISA does not require pension
20 plans to pay out any specific dollar amount, it does
21 regulate the rate at which benefits accrue. 29 U.S.C. §

1 1054(b)(1); see *Cent. Laborers' Pension Fund v. Heinz*, 541
2 U.S. 739, 743 (2004). Toward that end, ERISA sets forth
3 three alternative minimum benefit accrual tests; pension
4 plans are required to pass one. 29 U.S.C. § 1054(b)(1)(A)-
5 (C). Two of these tests are implicated by this appeal: the
6 133 1/3 test and the fractional test.

7 Under the 133 1/3 test, the rate of benefit accrual in
8 any future year may not be more than one-third greater than
9 the rate in the current year. 29 U.S.C. § 1054(b)(1)(B).
10 This test prevents "backloading" by cabining fluctuation in
11 accrual rates. As the Supreme Court explained, the 133 1/3
12 test "permits the use of any accrual formula as long as the
13 accrual rate for a given year of service does not vary
14 beyond a specified percentage from the accrual rate of any
15 other year under the plan." *Alessi v. Raybestos-Manhattan,*
16 *Inc.*, 451 U.S. 504, 514 n.9 (1981).

17 The fractional test "is essentially a pro rata rule
18 under which in any given year, the employee's accrued
19 benefit is proportionate to the number of years of service
20 as compared with the number of total years of service
21 appropriate to the normal retirement age." *Id*; see also 29

1 U.S.C. § 1054(b)(1)(C). In other words, this test uses a
2 fractional calculation based on years of service to ensure
3 that benefits accrue at a rate that approximates the
4 prorated amount of the total benefits that the employee
5 would receive if he or she worked until normal retirement
6 age. One unique feature of the fractional test formula is
7 that it uses the employee's current compensation rate to
8 project the total benefits available at retirement. This
9 means that the formula assumes *no* salary increases for the
10 employee.

11 Article 4.1(e) of the Citibuilder Plan sets forth its
12 mechanism for compliance with ERISA's minimum accrual
13 standards.⁴ Although the percentage of compensation that
14 Citigroup contributes to participants' accounts increases by
15 more than one third, based on increasing age and service
16 years, "the Plan may still qualify under the 133 1/3 percent
17 test because of the value of the interest credits compounded
18 annually through normal retirement age." *Esdén*, 229 F.3d at

⁴ The full text of Article 4.1 is set out in the district court's opinion. *In re Citigroup Pension Plan ERISA Litig.*, 470 F. Supp. 2d 323, 329-30 (S.D.N.Y. 2006) ("*Citigroup I*").

1 167 n.18. Compliance with the 133 1/3 percent rule depends
2 upon the balance between Benefit Credits, which increase
3 with age, and Interest Credits, which decrease with age.
4 Compliance is also contingent upon the variable interest
5 rate remaining sufficiently high to counterbalance the
6 increase in Benefit Credits with the decrease in Interest
7 Credits.

8 In order to ensure compliance, regardless of
9 fluctuations in the interest rate, Citigroup's Plan provides
10 that when the rate of accrual does not satisfy the 133 1/3
11 test, participants' accounts will be made to comply with the
12 fractional rule of accrual upon the termination of the
13 period of employment. If the variable interest rate falls
14 to a level at which compliance with the 133 1/3 test is not
15 possible, Citigroup will calculate the minimum account
16 requirements pursuant to Article 4.1(e) and then add the
17 difference to the participants' accounts. Under the
18 interest rates in effect in 2000 and 2001, the Plan was in
19 compliance with the 133 1/3 test, and neither Article 4.1(e)
20 nor the fractional test was implicated. However, beginning
21 in 2002, a change in the interest rate brought the Plan out

1 of compliance with the 133 1/3 test for some participants.
2 Article 4.1(e) was invoked with respect to the affected
3 participants in order to bring the Plan into compliance with
4 ERISA's minimum accrual rules.

5 **D. ERISA's Notice Requirement**

6 In order to safeguard benefits promised to employees
7 and to ensure that employees can form realistic expectations
8 about the benefits that they will receive, ERISA prohibits
9 employers from reducing the accrual of future benefits
10 without adequate notice to plan participants. See *Frommert*
11 *v. Conkright*, 433 F.3d 254, 263 (2d Cir. 2006). At all
12 times relevant to the amendments at issue on this appeal,
13 ERISA § 204(h) provided that a pension plan:

14 may not be amended so as to provide for a
15 significant reduction in the rate of future
16 benefit accrual, unless, after adoption of
17 the plan amendment and not less than 15
18 days before the effective date of the plan
19 amendment, the plan administrator provides
20 a written notice, setting forth the plan
21 amendment and its effective date, to . . .
22 each participant in the plan.

23
24 29 U.S.C. § 1054(h).⁵

⁵ The statute was subsequently amended, but it is this version that controls in this appeal. See Pub. L. No. 107-16, § 659(b), 115 Stat. 38, 139-41 (2001).

1 Guidelines promulgated by the Internal Revenue Service
2 (“IRS”) clarify that notice is required when an amendment is
3 “reasonably expected to change the amount of the future
4 annual benefit commencing at normal retirement age.” Notice
5 of Significant Reduction in the Rate of Future Benefit
6 Accrual, 63 Fed. Reg. 68,678, 68,680 (Dec. 14, 1998)
7 (codified at 26 C.F.R. pts. 1, 602). Whether an amendment
8 creates a “significant reduction” in accrual rates is
9 determined “based on reasonable expectations taking into
10 account the relevant facts and circumstances at the time the
11 amendment is adopted.” *Id.* at 68,681. According to the IRS
12 guidelines, notices may contain “a summary of the amendment,
13 rather than the text of the amendment, if the summary is
14 written in a manner calculated to be understood by the
15 average plan participant.” *Id.* at 68,682; *see also Register*
16 *v. PNC Fin. Servs. Group, Inc.*, 477 F.3d 56, 72 (3d Cir.
17 2007).

18 **II. PROCEEDINGS IN THE DISTRICT COURT**

19 Plaintiffs filed consolidated actions on behalf of
20 themselves and a class of similarly situated individuals
21 against Citigroup and its Plan’s Administration Committee,

1 alleging that the Citibuilder Plan violates ERISA. *In re*
2 *Citigroup Pension Plan ERISA Litig.*, 470 F. Supp. 2d 323,
3 326 (S.D.N.Y. 2006) ("*Citigroup I*"). Plaintiffs seek
4 injunctive and declaratory relief as well as monetary
5 damages. Plaintiffs allege, among other things, that the
6 Plan is impermissibly backloaded due to insufficient
7 Interest Credits; that the Plan's fractional test method of
8 computing accrued benefits is precluded under ERISA; and
9 that Defendants failed to provide Plan participants with
10 adequate notice that the 2000 and 2002 cash balance
11 amendments would reduce the rate of future benefit accrual.
12 *Id.* at 326-27.

13 On December 12, 2006, on cross-motions for summary
14 judgment, the district court denied Defendants' motion for
15 summary judgment and granted Plaintiffs' motion in part.
16 *Id.* at 327. The court ruled, in relevant part, that, as a
17 matter of law, the Plan violated ERISA's minimum benefit
18 accrual rules, 29 U.S.C. § 1054(b)(1)(A)-(C); and, that the
19 Plan violated ERISA's requirement that Plan administrators
20 provide advance notice of significant reductions in the rate
21 of future benefit accrual, as set out in 29 U.S.C. §

1 1054(h). *Id.* at 337-40.

2 The district court concluded that “[b]y its very terms,
3 the fractional rule may only be applied to participants with
4 ten or fewer years of service,” and that “the only
5 applicable accrual test is the 133 1/3 rule” because
6 Citigroup utilizes a “career average plan.” *Id.* at 337.
7 The court went on to opine that the “Citigroup formula . . .
8 contravenes the well-acknowledged purpose of the mandatory
9 accrual tests, which is to prevent the backloading of
10 benefits.” *Id.* at 337-38.

11 With respect to the § 204(h) notices provided by
12 Citigroup, the district court found that they “omitted any
13 mention of the benefit formula’s unorthodox approach to
14 calculating benefits and monitoring accrual rates,” and that
15 “defendants’ failure to either include or summarize Article
16 4.1(e) in the notices violated § 204(h).” *Id.* at 339. The
17 district court found that the notice provided was
18 “substantively inadequate,” and rejected Defendants’
19 argument that the notice claims should be “dismissed for
20 plaintiffs’ failure to show that they suffered any
21 prejudice.” *Id.* at 339-40 & n.88.

1 By Opinion and Order dated December 19, 2006, the
2 district court certified a class of plaintiffs consisting of
3 all individuals who were participants in the Plan at any
4 time on or after January 1, 2000, their beneficiaries and
5 estates, and those who are currently subject to the Plan's
6 cash balance formula under ERISA. *In re Citigroup Pension*
7 *Plan ERISA Litig.*, 241 F.R.D. 172 (S.D.N.Y. 2006).

8 On April 4, 2007, the district court clarified its
9 summary judgment ruling with respect to its finding that
10 Defendants had provided inadequate § 204(h) notice. *In re*
11 *Citigroup Pension Plan ERISA Litig.*, No. 05-cv-5296 (SAS),
12 2007 WL 1074912 (S.D.N.Y. Apr. 4, 2007) ("*Citigroup II*").
13 The court concluded that application of the fractional test
14 under the Citigroup Plan was a "deliberate end-run around
15 statutory guidelines that effectively kept the Plan's
16 accrual rates below the minimum prescribed by Congress."
17 *Id.* at *3. The court held that "[i]nsofar as [its] ruling
18 [of December 12, 2006] suggests that the § 204(h) notices
19 were required to describe how the amendments were going to
20 reduce rates of benefit accrual, their lack of detail was of
21 secondary importance to their material omission of an

1 unorthodox yet vital component of the Plan's formula." *Id.*
2 at *4. The court stated "that had the notices merely
3 identified the Plan's novel compliance mechanism, those few
4 words would likely have been adequate." *Id.* However,
5 because the notice omitted this information, the court's
6 prior conclusion that it was defective remained unchanged.
7 *Id.* On appeal, Plaintiffs contend that this "clarification"
8 constitutes an abuse of discretion on the part of the
9 district court because it prejudiced their notice arguments
10 without an opportunity to be heard.

11 On November 20, 2007, the district court issued a
12 ruling directing Defendants to adjust the Plan formula in a
13 manner that would bring it into full compliance with the 133
14 1/3 minimum benefit accrual test. *In re Citigroup Pension*
15 *Plan ERISA Litig.*, No. 05-cv-5296 (SAS), 2007 WL 4205855, at
16 *3 (S.D.N.Y. Nov. 20, 2007) ("*Citigroup III*"). The court
17 rejected Plaintiffs' arguments that further relief was
18 appropriate on the backloading and notice claims. *Id.*

19 Pursuant to Federal Rule of Civil Procedure 54(b), the
20 district court entered final judgment on the backloading and
21 notice claims, and simultaneously stayed enforcement of that

1 judgment pending this appeal. Defendants appeal from those
2 portions of the final judgment that find violations of
3 ERISA's minimum benefit accrual and notice provisions.
4 Plaintiffs thereafter cross-appealed from the final
5 judgment.

6 **III. DISCUSSION⁶**

7 **A. The Fractional Rule May be Applied to Cash**
8 **Balance Plans**

9
10 The district court concluded that the fractional test
11 can never be applied to career average plans like the cash
12 balance plan at issue in this case. The court determined
13 that "[b]y its very terms, the fractional rule may only be
14 applied to participants with ten or fewer years of service."
15 *Citigroup I*, 470 F. Supp. 2d at 337. On appeal, both
16 Citigroup and Plaintiffs agree that a fractional test may
17 legally be applied to a cash balance plan without violating
18 ERISA's minimum benefit accrual rules. The American

⁶ It is well known that we review a grant of summary judgment *de novo*. *State St. Bank & Trust Co. v. Salovaara*, 326 F.3d 130, 135 (2d Cir. 2003). When, as in this case, there are no material facts in dispute, this court is charged with making a determination as to whether the district court properly applied the relevant law. *McDonald v. Pension Plan of the NYSA-ILA Pension Trust Fund*, 320 F.3d 151, 155 (2d Cir. 2003).

1 Benefits Council, as *amicus curiae*, joins this position. In
2 our view, the position now advanced by all the litigants and
3 the *amicus curiae* is the correct interpretation of ERISA.
4 Contrary to the conclusion of the district court, ERISA §
5 204(b) provides that all defined benefit plans may use any
6 of the three minimum accrual tests to comply with anti-
7 backloading rules. 29 U.S.C. § 1054(b)(1)(A)-(C).

8 The fractional rule does not, in fact, state that it
9 may only be applied to participants with ten or fewer years
10 of service.⁷ Rather, the rule notes only that in
11 calculating benefits owed, it “tak[es] into account no more
12 than the 10 years of service immediately preceding his
13 separation from service.” 29 U.S.C. § 1054(b)(1)(C). The
14 provision is an instruction as to how to perform the accrual
15 calculation, not a blanket prohibition on the types of plans
16 that can utilize the fractional rule. Further, compliance

⁷ Several district courts in other circuits have also adopted the district court’s interpretation. See, e.g., *Wheeler v. Pension Value Plan for Employees of Boeing Co.*, No. 06-cv-500 (DRH), 2007 WL 2608875, at *7 (S.D. Ill. Sept. 6, 2007); *Sunder v. U.S. Bank Pension Plan*, No. 05-cv-01153 (ERW), 2007 WL 541595, at *11 (E.D. Mo. Feb. 16, 2007); *Eaton v. Onan Corp.*, 117 F. Supp. 2d 812, 843 (S.D. Ind. 2000). But, for the reasons discussed in this opinion, we find it unpersuasive.

1 with the fractional rule is tested "upon [the employee's]
2 separation from [the employer's] service," not, as the
3 district court concluded, on a "year-by-year basis." 26
4 U.S.C. § 411(b)(1)(C); 29 U.S.C. § 1054(b)(1)(C); *Citigroup*
5 *I*, 470 F. Supp. 2d at 338.

6 Congress has authorized the IRS to issue binding
7 regulations under ERISA, and we have noted that these
8 regulations "represent[] the fair and considered judgment of
9 the IRS" and are therefore "entitled to deference." *Esdén*,
10 229 F.3d at 168; see also Notice of Significant Reduction in
11 the Rate of Future Benefit Accrual, 68 Fed. Reg. 17,277
12 (Apr. 9, 2003) (codified at 26 C.F.R. pts. 1, 54 & 602). In
13 fact, the IRS "was given primary jurisdiction and rule-
14 making authority over ERISA's funding, participation,
15 benefit accrual and vesting provisions." *Esdén*, 229 F.3d at
16 157 n.2. Both the IRS regulations and Revenue Ruling 2008-7
17 contain an example of a defined benefit plan tested under
18 the fractional rule where the plan's benefit formula takes
19 into account more than ten years of employment. See 26
20 C.F.R. § 1.411(b)-1(b)(3)(iii)(Ex. 2); Rev. Rul. 2008-7,
21 2008-7 I.R.B. 419; see also I.R.S. Notice 96-8, 1996-1 C.B.

1 359 (Jan. 18, 1996) (stating that cash balance plans may
2 comply by utilizing any one of the three minimum accrual
3 tests). Thus, the district court erred in concluding that
4 application of the fractional test is *per se* illegal in the
5 context of cash balance plans.

6 **B. Application of the Fractional Test to the**
7 **Citibuilder Cash Balance Plan Does Not Violate**
8 **ERISA's Minimum Benefit Accrual Rules**
9

10 The district court concluded that under ERISA, benefits
11 must accrue in a way so that in any given year, the amount
12 of accrued benefit complies with the fractional rule's
13 minimum standards. Article 4.1(e) of the Citibuilder Plan
14 calls for the compliance calculation to occur when benefits
15 are paid out. If, on the determination date, the amount of
16 accrued benefit does not meet the fractional test, Citigroup
17 adds money to the account to bring it into compliance with
18 the minimum accrual requirements. Plaintiffs argue that
19 this amounts to impermissible backloading. The district
20 court characterized Article 4.1(e) as "unorthodox," and
21 agreed with Plaintiffs that it was a "novel end-run around
22 ERISA's minimum accrual standards." *Citigroup I*, 470 F.
23 Supp. 2d at 337-38. We disagree; the text of ERISA dictates

1 a different result.

2 The provision governing the fractional rule states that
3 a defined benefit plan, which includes a cash balance plan,
4 "satisfies the requirements of this paragraph if the accrued
5 benefit to which any participant is entitled *upon his*
6 *separation* from the service is not less than a fraction of
7 the annual benefit commencing at normal retirement age to
8 which he would be entitled under the plan as in effect on
9 the date of his separation." 29 U.S.C. § 1054(b)(1)(C)
10 (emphasis added). Thus, by its own language, the fractional
11 rule indicates that the relevant calculations are to be made
12 at the time of separation.

13 The statute's plain language is in accord with the
14 purpose of the minimum benefit accrual rules. Minimum
15 benefit accrual rules under ERISA are designed to prevent
16 participants who leave their employment before normal
17 retirement age from receiving benefits that are
18 disproportionately low relative to benefits they would have
19 received if they had continued to work until normal
20 retirement age. See, e.g., *Langman*, 328 F.3d at 71; *Hurlic*
21 *v. S. Cal. Gas Co.*, 539 F.3d 1024, 1033 (9th Cir. 2008).

1 The fractional test employed by Article 4.1(e) accomplishes
2 this statutory objective by guaranteeing departing employees
3 a benefit proportional (based upon years of service) to the
4 benefit they would have received had they worked until
5 normal retirement age. Under this test, adjustments are
6 made to departure-time benefits to ensure that the
7 participant is not penalized for leaving prior to normal
8 retirement age. The rate of benefit accrual during a
9 participant's employment is unimportant under this test, as
10 long as proportional benefits are paid at the time of
11 departure.

12 Revenue Ruling 2008-7 is instructive in the case at
13 bar; it provides an example in which it first tests the plan
14 using the 133 1/3 percent method and finds it satisfied for
15 some, but not for all, participants. Rev. Rul. 2008-7. The
16 example provided by the Revenue Ruling then applies the
17 fractional rule to those participants for whom the plan did
18 not satisfy the 133 1/3 test. *Id.* The Ruling specifically
19 states that this is "not a classification that is structured
20 to evade the accrued benefit requirements of § 411(b)(1)(A),
21 (B), and (C) or § 1.411(b)-1." *Id.* Again, this court has

1 noted that “[r]evenue rulings issued by the I.R.S. are
2 entitled to great deference, and have been said to have the
3 force of legal precedent unless unreasonable or inconsistent
4 with the provisions of the Internal Revenue Code.”

5 *Gillespie v. United States*, 23 F.3d 36, 39 (2d Cir. 1994)
6 (quotation marks omitted). Here, the Revenue Ruling
7 provides a reasonable interpretation of the statutory
8 language. Therefore, we hold that Article 4.1(e)’s
9 application of the fractional test at the time of separation
10 from employment is proper, and that it achieves the purposes
11 of ERISA’s minimum benefit accrual rules.

12 **C. Citigroup Complied with ERISA’s § 204(h)**
13 **Notice Requirements**

14
15 In its original opinion, the district court incorrectly
16 reasoned that because the notices given by Citigroup
17 “omitted any mention of the benefit formula’s unorthodox
18 approach to calculating benefits and monitoring accrual
19 rates,” and because the court ultimately concluded that the
20 formula violated ERISA, “defendants’ failure to either
21 include or summarize Article 4.1(e) in the notices violated
22 § 204(h).” *Citigroup I*, 470 F. Supp. 2d at 339.
23 Essentially, the district court converted a perceived

1 substantive defect in the Plan into a basis for finding that
2 the notice given was defective. The district court
3 recognized this error and attempted to cure it in its
4 Memorandum Opinion and Order of April 4, 2007. The court
5 suggested "that had the notices merely identified the Plan's
6 novel compliance mechanism," and presumably alerted the
7 participants to the existence of Article 4.1(e), they would
8 have been sufficient. *Citigroup II*, 2007 WL 1074912, at *4.
9 But, because the notice did not provide participants with
10 this information, the lower court still found that it failed
11 to comply with ERISA § 204(h). *Id.* We disagree with both
12 of the district court's formulations of ERISA's § 204(h)
13 notice requirements, and find that the Citibuilder Plan
14 Administrator complied with ERISA § 204(h).

15 As an initial matter, we reject Citigroup's argument
16 that Plaintiffs lack standing to maintain a notice claim
17 under § 204(h). The cases Citigroup cites for this
18 contention are inapposite; they discuss ability to maintain
19 a claim pertaining to the statutory requirement to provide a
20 Summary Plan Description ("SPD"). *See, e.g., Weinreb v.*
21 *Hosp. for Joint Diseases Orthopaedic Inst.*, 404 F.3d 167,

1 170 (2d Cir. 2005) (citing 29 U.S.C. §§ 1021(a), 1022(a)-
2 (b), and 1024(b)). ERISA specifically sets out the
3 information that must be contained in a SPD. 29 U.S.C. §
4 1022(b). "Among other things, [the] SPD must set out the
5 'circumstances which may result in disqualification,
6 ineligibility, or denial or loss of benefits.'" *Wilkins v.*
7 *Mason Tenders Dist. Council Pension Fund*, 445 F.3d 572, 580-
8 81 (2d Cir. 2006) (quoting 29 U.S.C. § 1022(b)). This
9 circuit has held that to prevail on a claim alleging that a
10 SPD provided deficient notice, a plaintiff must show that he
11 or she was "likely to have been harmed," or prejudiced.
12 *Burke v. Kodak Ret. Income Plan*, 336 F.3d 103, 113 (2d Cir.
13 2003). To apply this "likely prejudice" standard in this
14 case would be to conflate the requirements for bringing a
15 claim challenging the sufficiency of a SPD under 29 U.S.C. §
16 1024(b) with those governing the provision of notice under
17 29 U.S.C. § 1054(h). See *Burke*, 336 F.3d at 113-14.

18 Notice of an amendment to a pension plan "need not
19 contain an exact quotation of the text of the amendment, but
20 may contain 'a summary of the amendment . . . if the summary
21 is written in a manner calculated to be understood by the

1 average plan participant and contains the effective date.’’
2 *Register*, 477 F.3d at 72 (quoting *Scott v. Admin. Comm. of*
3 *the Allstate Agents Pension Plan*, 113 F.3d 1193, 1200 (11th
4 Cir. 1997) (quoting 26 C.F.R. § 1411(d)-6T (1996))).⁸ The
5 notices distributed by Citigroup to all Plan participants
6 properly provided a general summary of how the cash balance
7 plan would function. See *Osberg v. Footlocker, Inc. &*
8 *Footlocker Ret. Plan*, - F. Supp. 2d -, No. 07-cv-1358 (DAB),
9 2009 WL 2971834, at *9 (S.D.N.Y. Sept. 16, 2009) (discussing
10 applicable version of ERISA § 204 and concluding that it
11 “required the disclosure of only the amendment and its
12 effective date, and did not seek to regulate the content of
13 the communication any further”).

14 ERISA does not require that notice pursuant to § 204(h)
15 include a description of how the plan will comply with
16 minimum benefit accrual rules. The Citigroup 1999 and 2001

⁸ Congress amended ERISA in 2002 to provide that an amendment must “be written in a manner calculated to be understood by the average plan participant and shall provide sufficient information . . . to allow applicable individuals to understand the effect of the plan amendment.” 29 U.S.C. § 1054(h)(2). We express no view on whether notice given by Citigroup would satisfy current law. Rather, we analyze the law in effect at the time relevant to Plaintiffs’ challenge.

1 Notices properly alerted Plan participants that the
2 amendments could result in a reduction in rates of benefit
3 accrual. The Notices also made disclosures regarding the
4 Benefit Credit formula and Plan interest rate, which
5 permitted participants to compare this formula to their
6 prior benefits formula. Section 204(h) only requires notice
7 of plan amendments that "provide for a significant reduction
8 in the rate of future benefit accrual." 29 U.S.C. 1054(h).
9 Article 4.1(e) does not, in and of itself, reduce
10 participants' benefits. Rather, it increases benefits when
11 necessary to ensure compliance with ERISA's minimum accrual
12 rules. The participants had proper notice that the
13 conversion to a cash balance plan could have the effect of a
14 reduction of rates of benefit accrual. The 1999 and 2001
15 Notices complied with the requirements of ERISA § 204(h).

16 **IV. CONCLUSION**

17 Based on the foregoing analysis, the district court's
18 order of December 11, 2006, granting partial summary
19 judgment to Plaintiffs, is hereby REVERSED and the complaint
20 is DISMISSED.