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Benefits Alert

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Pension plan de-risking transactions targeted by plaintiffs' bar

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Defined benefit plan administrators considering de-risking transactions should be aware of the new challenge by plaintiffs.

What's the impact?

- If these cases move past a motion to dismiss, there is a high risk that similar cases will follow, particularly if the annuity provider is not a traditional insurer.
- The Courts of Appeals, or even the Supreme Court, may need to weigh in before Article III standing in these new pension risk transfer transaction cases is resolved.
- If the lower courts rule that allegations of an annuity provider being "too risky" or "non-traditional" are enough to satisfy Article III standing, it is likely that additional annuity providers will be targeted, and additional large pension risk transfer transactions will be challenged in class actions.

Recently, two plaintiffs' firms brought Employee Retirement Income Security Act (ERISA) class actions over the "de-risking" of defined benefit plan pension benefits—claims that were long thought put to rest due to lack of Article III standing. Specifically, Lockheed Martin and AT&T were sued for breaches of ERISA fiduciary duties for contracting with an allegedly risky annuity provider to pay employee pension benefits, arrangements often referred to as pension de-risking or pension risk transfer (PRT) transactions.

What's alleged in each class action complaint?

There are dueling class action complaints against AT&T in the United States District Court for the District of Massachusetts—*Piercy v. AT&T Inc.*(*Piercy* Complaint) and *Schloss v. AT&T, Inc.*(*Schloss* Complaint).[1] These cases allege that AT&T "offloaded" over $8 billion of pension liabilities for 96,000 AT&T defined benefit plan participants (AT&T participants) to Athene Annuity and Life Company and Athene Annuity & Life Assurance Company of New York (collectively Athene).

The *Piercy* Complaint alleges three claims against AT&T—one for breaching its ERISA fiduciary duties in choosing Athene as the annuity provider and two for prohibited transactions. In addition, the Plaintiffs seek an order requiring AT&T to guarantee the Athene annuities by purchasing "appropriate guarantees from reliable insurers selected through appropriate procedures, or the posting of an appropriate security."

The *Schloss* Complaint alleges three ERISA breach claims: (1) AT&T acted imprudently by not choosing the safest annuity provider, (2) AT&T engaged in a prohibited transaction, and (3) AT&T failed to adequately monitor the specific fiduciaries who picked Athene. Plaintiffs also ask the court to order AT&T "to post adequate security to assure receipt by Plaintiffs and class members of all retirement benefits covered by Athene annuities, plus prejudgment interest."

The third case, *Konya v. Lockheed Martin, Corp.* (*Lockheed* Complaint),[2] alleges that Lockheed Martin "offloaded" $9 billion in pension obligations to Athene to pay the pension benefits for 31,000 defined benefit plan participants. The *Lockheed* Complaint alleges the same three claims and relief as the *Schloss* Complaint and was brought by the same law firm.

COMMON THEMES IN THESE ERISA CLASS ACTIONS

Relying on the Department of Labor's Interpretive Bulletin 95-1,[3] which provides guidance relating to ERISA's fiduciary standards regarding the selection of an annuity provider for defined benefit pension liabilities, the complaints claim that AT&T and Lockheed were required to choose the "safest annuity available" but did not do so. The three complaints generally allege that Lockheed Martin and AT&T chose a risky annuity provider—Athene—to take over their pension obligations and that in shifting the pension obligations to an annuity provider, the employees lost ERISA's protections. According to plaintiffs, this puts the employees' future pension benefits

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[1] *Piercy v. AT&T Inc.*, Case No. 1:24-cv-10608 (Mar. 11, 2024, D. Mass.); *Schloss v. AT&T, Inc.*, 1:24-cv-10656 (Mar. 15, 2024, D. Mass.).

[2] *Konya v. Lockheed Martin, Corp.*, 8:24-cv-00750 (Mar. 13, 2024, D. Md.).

[3] 29 CFR § 2509.95-1.

at risk of default, which allegedly constitutes a devaluation of their pensions for which they were not compensated. There is, however, no allegation in any of the complaints that participants are not receiving their vested benefits.

The complaints focus on an allegation that Lockheed Martin and AT&T chose a non-traditional PRT annuity provider rather than a well-known and established insurance company. According to the allegations, Athene is owned by a private equity firm and has a subsidiary, Athene Life Re (ALR), that is an offshore captive reinsurer headquartered in Bermuda. Plaintiffs allege that Athene is dependent on ALR and, thus, has a far riskier asset base than other conventional annuity providers, and on that basis, claim that these PRT transactions have put plan participants at risk of losing their pension benefits.

Developments to watch

In the coming months, we expect defendants to file motions to dismiss based on lack of standing and the speculative nature of the allegations. In the last major de-risking case, *Lee v. Verizon Communications Inc.*,[4] the Court of Appeals for the Fifth Circuit in 2016 threw out a challenge to Verizon's $7.4 billion PRT transaction because it found, among other things, that the plaintiffs failed to adequately allege that plan participants suffered the kind of harm that Article III of the US Constitution requires to establish standing. To meet that requirement, plaintiffs must allege facts to support that they have suffered an injury that is "concrete and particularized" and "actual or imminent, not conjectural or hypothetical." If the claim is based on a future harm, there must be a substantial risk that the harm will occur.

In *Verizon,* two classes were certified: the transferee class, whose $7.4 billion in benefit obligations were transferred outside the plan when Verizon entered into the PRT, and the non-transferee class, whose benefits remained in the plan. The transferee class sued for breach of fiduciary duty, claiming, among other things, that the fiduciary acted imprudently by placing the entire annuity purchase with one insurer instead of spreading it among several, which was too risky. The district court dismissed the transferee class's claims under Rule 12(b)(6) for failure to state a claim under ERISA, which the Fifth Circuit affirmed.

The non-transferee class separately sued for breach of fiduciary duty, claiming that the $8.4 billion in plan assets that Verizon paid in satisfaction of the transferee class's $7.4 billion of benefit obligations included $1 billion for payment of the annuity provider's fees. The non-transferee class alleged these fees were excessive and imprudently caused the plan's funding level to drop to 66%. The district court dismissed the claim for lack of constitutional standing.

The Fifth Circuit, consistent with other Circuits in analogous circumstances, held that standing in defined benefit plan cases requires the plaintiff to allege either actual default or imminent risk of default by the plan "such that the participant's benefits are adversely affected" and that

[4] *Lee v. Verizon Communications Inc.*, 837 F.3d 523 (5th Cir. 2016).

anything less is "too speculative." This is because participants in defined benefit plans have a right to receive a particular benefit amount under the plan's formula, regardless of whether the plan's trust is fully funded. The court concluded that the non-transferee class failed to meet this standard because the plan was still ongoing and Verizon would be obligated to make up any shortfall in funding. In addition, even if Verizon were to collapse, the federal Pension Benefit Guaranty Corporation (the FDIC of pensions) would be required to provide backstop coverage. The court emphasized that the plaintiff "does not allege a plan termination" or "an inability by Verizon to address a shortfall in the event of a [plan] termination."

The Supreme Court later cited *Lee v.* Verizon favorably in *Thole v. U.S. Bank N.A.*, affirming that more than "a bare allegation of plan underfunding" is required to plead "a substantially increased risk that the plan and the employer would both fail."[5]

Will courts determine the future of PRT transactions?

The *Piercy*, *Schloss*, and *Lockheed* complaints appear designed to try to get around *Lee v. Verizon* and *Thole* by alleging that the PRT transactions concluded in the transfer of affected participants out of their retirement plans to a risky annuity provider, accompanied by the loss of two ERISA protections: (1) the availability of AT&T's and Lockheed's assets to help pay for benefits if the plans' funding levels fall precipitously and (2) the availability of the PBGC's benefit guarantee if AT&T and Lockheed collapse. The *Schloss* and *Lockheed* complaints also allege that loss of the PBGC's benefit guarantee is particularly concerning because if the annuity provider fails, transferred participants have only the backstop of state insurance guaranty associations, whose guarantees are capped differently than the PBGC's. But those two ERISA regulatory features are always lost when a defined benefit pension plan is terminated in a "standard termination" that ERISA expressly authorizes. So, the only real question for the courts should be whether the "risky" and "non-traditional" annuity provider allegations are sufficient to move these cases out of the "too speculative" category discussed in *Lee v. Verizon* and *Thole* and into the "substantial risk of future harm" category necessary for Article III standing.

Given the stakes, we might not have much certainty until we hear from the Courts of Appeals or even the Supreme Court.

If you are considering a pension risk transfer, it is imperative to:

- Be mindful of potentially heightened litigation risk in light of these unanswered questions;
- Assess potential litigation risks in advance of any deal activity; and
- Determine how to best mitigate those risks in accordance with the unique circumstances of your plan and any potential deal activity.

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[5] *Thole v. U.S. Bank N.A.*, 140 S. Ct. 1615, 1621-22 (2020).

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