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The individual beneficiaries of each respective inherited IRA transferred from the Retirement Accounts were separately responsible for any tax liabilities relating to required minimum distributions from their inherited IRAs or the tax year subsequent to the year the inherited IRAs were established or the year of death if later (and all subsequent tax years). No income taxes or penalties for failure of the individual beneficiaries to take their required minimum distributions for the tax year subsequent to the year the inherited IRAs were established or the year of death if later (or any subsequent tax years) would be passed to the trust or the trustees.

Bruce J. McNeil, Esq.

Editor-in-Chief

Journal of Deferred Compensation, What Is A Top Hat Group Depends On Jurisdiction—Plans Should Use A Forum Selection Clause To Avoid Confusion, (Jul. 1, 2025)

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INTRODUCTION:

The Top Hat plan exception from the Employee Retirement Income Security Act (ERISA) is probably the most important requirement for nonqualified deferred compensation plans. That said, there is very little statutory or regulatory guidance on what exactly is the top hat group, which leaves it to the courts to set parameters.

The term "top hat" does not appear in the statute or its legislative history of ERISA. The statute exempts an unfunded plan "that is maintained primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees." [ERISA §§ 201(2), 301(a)(3), and 401(a)(1)]. It is unclear how or why that phrase came to be known as a top hat plan. Perhaps it is a reference to when wealthy men wore top hats when out on the town, like the character Rich Uncle Pennybags (aka Mr. Monopoly).

Likewise, neither ERISA nor Department of Labor (DOL) regulations define the term "select group of management or highly compensated employees." However, the Preamble to the Treasury regulations under Section 414(q) of the Internal Revenue Code (Code), that defines highly compensated employee for the purpose of qualified plans, specifically provides that the Treasury and the DOL agree that the meaning of "highly compensated employee" for purposes of Section 414(q) of the Code is not applicable to the determination of the meaning of the same phrase under ERISA. [*See* TD 8173, February 19, 1988]. The select group of management or highly compensated employees must be determined in the context of the particular facts and circumstances that apply to the employer.

The legislative history on the top hat exemption is also rather sparse. [*See, e.g., H.R. Rep. No. 93-1280, at 296 (1974); H.R. Rep. No. 93-533, at 4656 (1974) (Conf. Rep.)*] In 1990, the DOL set forth its interpretation of the purpose for the top hat exemption in DOL Opinion Letter 90-14A [*1990 WL 123933 (May 8, 1990)*] (1990 Opinion). It stated:

> *It is the view of the Department that in providing relief for top hat plans from the broad remedial provisions of ERISA, Congress recognized that certain individuals, by virtue of their position or compensation level, have the ability to affect or substantially influence, through negotiation or otherwise, the design and operation of their deferred compensation plan, taking into consideration any risks attendant thereto, and, therefore, would not need the substantive rights and protections of Title I [of ERISA].*

Due to this lack of specificity, much of the guidance on what is a top hat group has come from case law. Over the years there has been litigation over whether a particular plan is, in fact, a top hat plan exempt from much of ERISA. The reason the issue winds up in court is usually because a disgruntled participant is arguing that he or she is entitled to a bigger benefit from the plan because the plan is not a top hat plan and, therefore, violates ERISA. It is easy to recognize that if a plan that was designed to be exempt from ERISA's participation, vesting, funding, and fiduciary duty rules turns out to be subject to such rules, it will likely fail to meet those requirements. This would generally mean that the participants must vest earlier than provided for under the plan document. Cases have examined virtually every portion of the phrase "maintained primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees." Federal Appellate Circuit Courts have varying ways of analyzing the issue. Also, while it would appear that the factors of "primarily", "select group", "management" and "highly compensated" seem to be independent, courts often merge them in their analysis. We will examine each of these factors and the case law addressing them below. We will also see that the 1990 Opinion has led to a split in the federal circuits as to the test for top hat group status. We will then examine how a forum selection clause might be used to avoid the lack of certainty in the area.

Primarily.

The use of the word "primarily" raises an issue as to whether top hat plans must only consist of management or highly compensated employees, or just "primarily" cover such employees while also covering other employees. The statute's wording could be interpreted to mean that top hat plans must cover primarily management or highly compensated employees, but not all participants have to qualify as such. However, the DOL stated in Advisory Opinion 90-14A that "primarily" refers to the purpose of the plan, not the participant composition—*i.e.* top hat plans must be maintained primarily for the purpose of providing deferred compensation. This position essentially limits top-hat plans to only management or highly compensated employees.

Some courts agree with this interpretation, others do not. In *Callan v. Merrill Lynch & Co., Inc*., the District Court, for the Southern District of California stated, "although the Ninth Circuit has been silent on this issue, other courts have recognized that a plan may still be a top hat plan even if some non-management or non-highly compensated employees are allowed to participate. *See, e.g., Fishman v. Zurich Am. Ins. Co.*, 539 F. Supp.2 d 1036, 1043 n. 7 (N.D.Ill.2008); *Demery,* 216 F.3d at 289; *Belka v. Rowe Furniture Corp*., 571 F. Supp. 1249, 1253–54 (D.Md.1983). The court then held that the fact that the plaintiff, Callan, may not have been a member of the select group of management did not preclude the plan from being a top hat plan. It should be noted that this is an unreported case which is not binding precedent but only persuasive precedent.

Management.

What constitutes "management" has not been declared by the DOL. However, the mere fact that all the plan participants are management employees will generally not be enough to be a top hat plan. Many courts use the "select group" factor in conjunction with the "highly compensated" factor to limit the group to highly compensated management employees.

In *Carrabba v. Randalls Food Markets, Inc*., 38 F. Supp.2 d 468 (N.D. Tex. 1999), the district court found the plan was not a top hat plan despite being comprised entirely of management employees. Because "[a]ll levels of management were represented by the participants in the plan," the plan did not meet the other requirements necessary to be a top hat plan. The court stated that "[t]he words 'a select group of' must be given some meaning," and that it "cannot find from the evidence that the participants of the MSP were 'a select group' out of the broader group of management employees or the broader group of highly compensated employees." In that case, all salaried employees were managers eligible to participate in the plan.

In *Bakri v. Venture Mfg. Co*., 473 F.3d 677, (6th Cir. 2007), the United States Court of Appeals for the Sixth Circuit found a plan was not a top hat plan where the plan covered employees with no supervisory, policy making, or executive responsibilities, reversing the decision of the federal district court. The court held that the plan, therefore, failed to satisfy the select group requirement of ERISA. The lower court had held the plan was a top hat plan even though four of the eight managers it covered had 2002 annual salaries ranging from $42,000 to $51,000 (including plaintiff, whose annual salary was $51,000). The plan covered between 25% and 50% of the company's management employees, though not the very highest-paid employees such as the owner-employees. The highest-paid employee had a salary of $118,313.

In *Accardi v. IT Litig. Trust*, 448 F.3d 661 (3d Cir. 2006), the United States Court of Appeals for the Third Circuit upheld the district court ruling that an elective deferred compensation plan was a top hat plan where it limited the group to employees selected by the company who had a base annual salary of at least $100,000, a level the district court concluded satisfied the highly compensated criteria for a top hat plan. The district court also upheld the Bankruptcy Court's finding that the plan satisfied the management requirement, stating that "[e]xecutive level seniority is not required; 'management' level is sufficient." *IT Group, Inc. v. Bookspan (In re IT Group, Inc.)*, 305 B.R. 402, 2 EXC 50, 32 EBC 2906 (Bankr. D. Del. 2004). In that case, the court found the lowest ranking grade of a participant was "E10: Human Resource Manager II." Additionally, nearly all of the jobs listed as participants contained the title "Manager," "Director," or "Controller."

These cases demonstrate the inconsistency among the Circuits. The Sixth Circuit appears to require supervisory, policy making, and executive responsibilities to be the management employees that can be part of the top hat group. On the other hand, the Third Circuit states that executive level is not required and appears to put a great emphasis on the title of the employee.

Highly Compensated Employees.

As noted above, the term "highly compensated employee" in the top hat plan context is not the same as that term is defined for discrimination purposes for qualified plans under Internal Revenue Code Section 414(q), which is currently $160,000 for 2025. Therefore, employers should not rely on the Code Section 414(q) definition of highly compensated employee when deciding who should participate in a top hat plan. On the other hand, an employee making less than the Section 414(q) dollar amount could be a highly compensated employee for top hat plan purposes, depending on the facts and circumstances. Likewise, an employee making well over the Section 414(q) dollar amount might not be a highly compensated employee for top hat purposes. In *Simpson v. Ernst & Young*, 879 F. Supp. 802 (S.D. Ohio 1994), the district court found a participant whose 1990 salary was $194,092 (well above the 414(q) number of $45,000 at the time) to not be highly compensated.

When analyzing who is a highly compensated employee for top hat plan purposes, caselaw generally compares the average compensation of the would-be top hat group plan participants to the average compensation of the employer's total work force. In *Simpson*, the court found that the participant was not highly compensated because "[a]lthough Simpson's 1990 salary was $194,092, this alone does not mean he was highly compensated when compared to the average compensation of Ernst & Young employees."

Conversely, in *Belka v. Rowe Furniture Corp.*, 571 F. Supp. 1249 (D. Md. 1983), the average salary of plan participants was only $55,000, but this was compared to the $16,000 average for all other employees. This difference of approximately 3½ times was sufficient for the Maryland district court to consider participants to be highly compensated. And in the seminal case, *Demery v. Extebank Deferred Compen. Plan (B)*, 216 F.3d 283 (2d Cir. 2000), the United States Court of Appeals for the Second Circuit found that "the average salary of plan participants was more than double that of the average salary of all Extebank employees. We find this did make them 'highly compensated'…." The DOL has even upheld a top hat plan with a mere one and a half times ratio. DOL Adv. Op. 75-64 (Aug. 1, 1975).

In *Duggan v. Hobbs*, 99 F.3d 307 (9th Cir. 1996), the United States Court of Appeals for the Ninth Circuit, held that the top salesman of a company, Duggan, who was the highest paid non-owner employee of the employer was a member of the select group and his deferred compensation plan providing for lifetime retirement benefits upon severance was a top hat plan. The court considered the policy behind the top hat exemption as announced by the DOL in the 1990 Opinion. The 1990 Opinion states that Congress recognized that certain individuals, by virtue of their positions or compensation level, have the ability to affect or substantially influence through negotiation or otherwise, the design and operation of their deferred compensation plan, taking into consideration any risks attendant thereto, and therefore, would not need the substantive rights and protection of Title I of ERISA. The court found that numerically Duggan qualified as a member of the select group because he was the only one of 23 employees participating in the plan (less than 5%). He also earned twice as much as the next highest paid employee and more than 4 times the average employee. However, the court stated the select group requirement includes more than a statistical analysis, as the DOL explained in the 1990 Opinion, the exception was intended to apply to employees who by virtue of their position or compensation level have the ability to affect or substantially influence, through negotiation or otherwise, the design and operation of the plan. Since Duggan exerted such influence through his attorney when negotiating the severance agreement, the severance agreement was maintained for a select group.

It's important to note that the *Duggan* court held that because Duggan exercised influence over the design of his plan and he was highly compensated, he was the type of employee that the top hat exemption was meant to cover and the plan a top hat plan. The court did not rule that in order to be a top hat plan all participants must have exercised influence over the design or even have the ability to exercise such influence.

However, other courts cite *Duggan* and the 1990 Opinion for the proposition that all participants must have such influence. This has caused a division in Federal Appellate Courts as to whether being highly compensated is enough or whether the participants must also be able to exert influence or bargaining power with respect to negotiating their benefits under the plan.

Courts continue to grapple with the issue of whether the top hat group must all have substantial influence or “bargaining power” to influence the design of their deferred compensation as alluded to by the *Duggan* decision. Some plaintiffs have maintained that the plan at issue could not qualify for the top hat exemption because the participants were not a sufficiently select group since they did not have the ability, or bargaining power, to affect or substantially influence the design and operation of the plan. Such cases required the courts to decide whether “substantial influence” or “bargaining power” is a substantive factor for a plan to be a top hat plan. As we’ll see below some courts have included “bargaining power” as a requirement while others emphatically hold there is no such requirement.

Select Group and Participant’s Bargaining Power.

The phrase “select group” limits the percentage of the workforce that can participate in a top hat plan. Unfortunately, there is no bright-line percentage cap. In *Demery v. Extebank Deferred Compen. Plan (B), 216 F.3d 283 (2d Cir. 2000),* the United States Court of Appeals for the Second Circuit found that a top hat plan offered to 15.34% of the company’s employees was valid, stating that “[w]hile this number is probably at or near the upper limit of the acceptable size for a ‘select group,’ we cannot say that it alone made Plan B too broad to be a top hat plan without considering the positions held at the bank by the Plan’s participants.” The percentage of employees covered by the plan needs to be sufficiently limited to be select. As will be seen below, courts will hold that if too many highly compensated or management employees are covered by the plan that it will not be sufficiently select.

Comparing the number of participants eligible for the plan to the total number of employees may not be the best measure of whether the plan covers a select group in all cases. For example, assume the employer is a fledgling C-corporation with only four employees: the President/CEO; 2 sales people; and a receptionist. If the corporation adopted a nonqualified deferred compensation plan to cover the President/CEO alone, the percentage of employees eligible for the plan would be 25%. Would this corporation be precluded from adopting a top hat plan until its workforce grew to lower the percentage to under 15.34%?

In *Duggan*, the court referenced 5% as a possible guideline, but also emphasized that each case must be analyzed individually because “the ‘select group’ requirement includes more than a mere statistical analysis.”

Other Circuits have cited the purpose of the top hat exemption as announced by the Department of Labor as *Duggan* did, in determining that the nature of the participants’ duties, including their bargaining power is a factor to be considered. In *Bakri,* the Sixth Circuit adopted a four-part test to determine top hat status reasoning that the court must consider both qualitative and quantitative factors. The four parts are: 1) the percentage of total workforce invited to join the plan (quantitative); 2) the nature of their employment duties (qualitative); 3) the compensation disparity between the top hat plan members and non-members (qualitative); and 4) the actual language of the plan (qualitative).

In 2015, a Pennsylvania district court answered the question of whether top hat group members must have bargaining power with a resounding no in *Sikora v. UPMC*, 153 F. Supp. 3 d 820 (W.D. Pa. 2015). The *Sikora* court specifically said that no appellate circuit court has held that “the ability or bargaining power to affect or substantially influence, through negotiation or otherwise, the design and operation of the plan is a required element of a top hat plan.” The *Sikora* case was appealed, and the United States Court of Appeals for the third circuit, upheld the lower court and specifically held that the DOL opinion letter was simply the Department’s explanation of why Congress created the top hat plan exception and there is no substantive requirement of substantial influence to be a top hat plan. *Sikora v. UPMC,* 876 F.3d 110, (3d Cir. 2017).

In so holding, the Third Circuit joined the First Circuit that in 2008 declined the plaintiff's invitation to go beyond the text of ERISA and "jerry-build onto it a requirement of individual bargaining power" in *Alexander v. Brigham and Women's Physicians Org., Inc.*, 513 F.3d 37 (1st Cir. 2008).

Other circuits seem to adopt substantial influence as a requirement, or at least, an important factor in determining top hat plan status. The Second, and Sixth Circuits view bargaining power as an important factor in the "select group" test. *Bakri v. Venture Mfg. Co.*, 473 F.3d 677, 678–79 (6th Cir. 2007); *Demery v. Extebank Deferred Compen. Plan (B)*, 216 F.3d 283 (2d Cir. 2000). A district court in the Fourth Circuit treated bargaining power as a "third requirement, set forth in DOL advisory opinions, that the select group consist of individuals who are in the position to protect their own interests." *Guiragoss v. Khoury*, 444 F. Supp. 2 d 649, 661 (E.D. Va. 2006).

The reasoning of the *Sikora* case makes the most sense, particularly when considering a plan of a large national corporation may have a large number of executive participants who individually would not have such bargaining power. However, there is a definite split in the federal circuits. This division makes the issue of whether substantial influence is a factor for top hat status chiefly depend on what jurisdiction a claim that the plan is not top hat is brought. This is not conducive to ERISA's goal of uniform law.

Can a Forum Selection Clause Avoid the Bargaining Power Issue?

One possibility to avoid the bargaining power issue coming up is to include in the plan document a forum selection clause adopting a federal district court in the Third or Sixth Circuit as the jurisdiction where any litigation must be brought.

In 2013, the United States Supreme Court held that a "contractually valid" forum selection clause should be enforced by federal courts absent extraordinary circumstances. *Atlantic Marine Construction Company v. United States District Court*, 571 U.S. 49, 134 S. Ct. 568 (2013). It didn't take long for a case involving a forum selection clause in an ERISA plan to be litigated. In 2014, the Sixth Circuit upheld a forum selection clause in an ERISA plan in *Smith v. Aegon Companies Pension Plan*, 769 F.3d 922, 931-933 (6th Cir. 2014). It was soon followed by decisions in the Seventh and Ninth Circuits in *In re Mathias*, 867 F.3d 727, (7th Cir. 2017) and *In re Becker*, 993 F.3d 731, (9th Cir. 2021), respectively. These courts all found that forum selection clauses in an ERISA plan are valid and should be upheld except in unusual or rare cases. In analyzing whether a forum selection clause should be upheld these courts considered the following factors: (1) whether the clause conflicts with provisions of ERISA regarding venue; and (2) whether the clause conflicts with ERISA's goal of providing ready access to federal courts.

ERISA's Venue Provision.

ERISA Section 1132(e)(2) provides: *Where an action under this subchapter is brought in a district court of the United States, it may be brought in the district where the plan is administered, where the breach took place, or where a defendant resides or may be found,* and process may be served in any other district where a defendant resides or may be found.

In *Smith*, the DOL submitted an amicus brief in support of the position that venue selection clauses were incompatible with ERISA. In that case, the plan was amended to include a venue selection clause requiring any lawsuit to be brought in federal district court in Cedar Rapids, Iowa. The participant sued to recover benefits under the plan in the Western District of Kentucky, but the suit was dismissed due to the plan's venue selection clause. The participant appealed and the United States Court of Appeals for the Sixth Circuit upheld the lower court's dismissal, finding that the venue selection clause was valid and enforceable because the venue selection language under ERISA does not preclude venue selection clauses. The court acknowledged that the language under ERISA is permissive, meaning suit *may* be brought in one of the listed venues and that the plan at issue provided that suit should be brought in one of the statutorily designated places. However, the court also recognized that "even if the venue selection clause laid venue outside of the three options provided by §1132, the venue selection clause would still control." *See Smith*, 769 F.3d at 932.

The position in *Smith* was affirmed by the Seventh Circuit in *Mathias*, where the Plan contained a forum selection clause requiring suit to be brought in a federal court in the Central District of Illinois. The participant brought his original suit in the Eastern District of Pennsylvania, where the district court granted defendant's motion to transfer the case to the Central District of Illinois. The participant moved to transfer the case back to Pennsylvania and the Illinois district court denied his motion. The participant then filed a writ of mandamus to order the lower court to transfer the case back to Pennsylvania. The United States Court of Appeals for the Seventh Circuit denied the participant's writ, adopting the Sixth Circuit's majority opinion in *Smith*, and finding that the plan's forum selection clause was valid and enforceable particularly because the plan chose a venue from among the venue options listed in ERISA and nothing in the statute invalidated such choice. It should be note that the DOL again filed an amicus brief in this case supporting the plaintiff's position that the forum selection clause was invalid under ERISA. However, the Seventh Circuit did not find the DOL's position persuasive.

In *Becker*, the Ninth Circuit aligned itself with the Sixth and Seventh Circuits, denying plaintiff's writ of mandamus attempting to vacate the lower court's order granting a motion to transfer from the Northern District of California to the District of Minnesota. The Ninth Circuit, citing *Mathias* and *Smith*, found that the text of ERISA was permissive and Congress "chose to open three venues for suit, but not to require them." *See Becker,* 993 F.3d at 732-733. The court recognized that the Plan in question chose one of the venues provided by the statute and that funneling litigation to a single federal court furthered ERISA's goals by encouraging uniformity in decisions interpreting the Plan. Ultimately, the court found that "courts are in near universal agreement: ERISA does not bar forum selection clauses" and had no reason to diverge from those court's "well-reasoned conclusions." *Id*.

***Access to Federal Courts*.**

These cases also considered whether a forum selection clause undermines ERISA's goal of allowing ready access to federal courts. In *Smith,* the participant and DOL argued that the Congressional policy of ready access to federal courts cannot be ignored. However, the Sixth Circuit found that neither "explains how a venue provision inhibits ready access to federal courts when it provides for venue in a federal court." It also found that other ERISA policies are furthered by venue selection clauses. It stated that, "limiting claims to one federal district encourages uniformity in the decisions interpreting that plan, which furthers ERISA's goal of enabling employers to establish a unform administrative scheme." *Smith* 769 F.3d 922, 931-932. It also found that it supports ERISA's goal of providing low-cost administration of employee benefit plans. *Id*.

Mathias adopted this reasoning of the Sixth Circuit in *Smith* stating, … "we find the majority's reasoning convincing. The Sixth Circuit's analysis is faithful to the statutory text and not inconsistent with the broader statutory policy of maintaining access to federal court." *Mathias,* 867 F.3d 727, at 732.

In *Becker,* the Ninth Circuit determined that the forum selection clause in question did not undermine ERISA's goal of allowing ready access to federal courts because it designated a federal court as the proper venue, guaranteeing that plaintiff's claim would be heard in federal court. *Becker*, 993 F.3d 731, 732-733. Additionally, the court noted that channeling all plan oversight through one federal court would result in uniformity in decisions interpreting the plan, which would benefit both administrators and beneficiaries by reducing plan costs ultimately fulfilling another goal of ERISA. *Id*. at 733.

It is clear from the above that forum selection clauses in ERISA plans are valid. It's important to note that the forum selected in the plans in *Smith*, *Mathias*, and *Becker* all fell within the three venue provisions under ERISA as an appropriate venue. However, the Smith court specifically said that choosing one of the venues listed in ERISA is not necessary.

CONCLUSION

Given the split in the federal circuits regarding the substantial influence/bargaining power issue raised by the 1990 Opinion for the meaning of the top hat group, a plan that can select a forum in the First or Third Circuit as the forum for litigation under ERISA Section 1132 would be prudent to do so. It should be noted that Delaware, where many corporations are incorporated, is in the Third Circuit. The Supreme Court has held that the state of incorporation of a corporation always has jurisdiction for a law suit. *See Ford Motor Co. v. Montana Eighth Jud. Dist. Ct.*, 592 U.S. 351, 358, 141 S. Ct. 1017, 1024, 209 L. Ed. 2d 225 (2021); *Daimler AG v. Bauman*, 571 U.S. 117, 118, 134 S. Ct. 746, 749, 187 L. Ed. 2d 624 (2014). This should be sufficient for a forum selection clause under ERISA Section 1132.

Under *Smith*, a forum can be selected that is outside of the ERISA Section 1132 choices. Therefore, it seems that plans whose forum selection would be litigated in that Circuit could select the First or Third Circuit to avoid the substantial influence/bargaining power issue.

Until the DOL changes its 1990 Opinion or the United States Supreme Court hears a case to resolve the split in the circuits, a forum selection clause may be the best way to avoid the bargaining power/substantial influence issue.

Journal of Deferred Compensation, Dobbs v Employee Benefits: Major Questions Left After the Landmark Decision, (Jul. 1, 2025)

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A committed advocate for the federal judiciary, Brendan serves as a national leader for the Federal Bar Association (FBA). He acts as a liaison to the Judiciary Division, regularly advocating on behalf of federal judges, and sits on the board of the FBA’s Civics, Service, and Outreach Committee, where he works to advance civics education in middle and high schools across the country. Brendan remains dedicated to community service, volunteering with local food banks and the Legal Aid Society of Cleveland, and as an Exchange Scholar for the National Constitution Center.

He is deeply grateful to his friends, family, and his fiancée, Chloe Reip, for their unwavering support. He also thanks ACEBC for its continued commitment to mentoring and supporting young scholars interested in ERISA and employee benefits.

I INTRODUCTION

On Monday, May 2, 2022, Politico released a report that it had obtained a copy of a draft opinion in the *Dobbs* case—an unprecedented event that shattered the Supreme Court’s long-held traditions of secrecy and confidentiality.[1] The leaked Supreme Court draft opinion of *Dobbs v. Jackson Women’s Health Organization*,