401(k) Litigation After LaRue v. DeWolff

Minimizing Exposure and Defending Claims Over
401(k) Plan Administration

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I. <u>The Supreme Court's Decision</u>

A. Background

1. The District Court decision

2. The Fourth Circuit Opinions

B. Majority Opinion

1. Holding: individual plan participants may sue for losses to their individual plan accounts irrespective of whether a recovery for such losses would benefit the plan as a whole

2. The majority's "changing landscape" rationale and the Court's new interpretation of *Massachusetts v. Russell*

3. Measuring the potential recovery in such claims

4. Open procedural issues

C. The Chief Justice's Concurring Opinion

D. Justice Thomas' Concurrence

II. <u>Broader Implications</u>

A. Standing of Former Participants to Sue for Fiduciary Violations

1. Typical fact pattern: Employee participated in Employer's 401(k) plan while employed by Employer. Her employment terminates, and she withdraws all of the assets in her account in Employer's plan (e.g., roll-over to an IRA). Post-withdrawal, does she qualify as a "participant" with standing to sue under ERISA § 502(a)(2) or § 502(a)(3)?

2. *LaRue*

a. Facts: Petitioner terminated his employment in 2001 but kept his funds in his account in the plan. He ultimately filed his *cert.* petition in November 2006. While the case was pending before the Fourth Circuit, however, Petitioner withdrew all of his funds from his account in the plan.

b. After *cert.* was granted, Respondents discovered the withdrawal, and moved to dismiss the writ. That motion was denied without opinion before oral argument.

c. The Court's opinion, at 128 S.Ct. 1026 n.6:

> After our grant of certiorari respondents filed a motion to dismiss the writ, contending that the case is moot because petitioner is no longer a participant in the Plan. While his withdrawal of funds from the Plan may have relevance to the proceedings on remand, we denied their motion because the case is not moot. A plan "participant," as defined by § 3(7) of ERISA, 29 U. S. C. §1002(7), may include a former employee with a colorable claim for benefits. See, e.g., *Harzewski v. Guidant Corp.*, 489 F. 3d 799 (CA7 2007).

3. The statute and *Bruch*:

a. ERISA § 3(7): "any employee or former employee of an employer . . . who is or may become eligible to receive a benefit of any type from an employee benefit plan which covers [such employees], or whose beneficiaries may be eligible to receive any such benefit."

b. *Firestone Tire & Rubber Co. v. Bruch*, 489 U.S. 101, 117-18 (1989): in the context of ERISA's plan document disclosure provisions, the term "participant" includes any "former employees who 'have' . . . 'a colorable claim' to vested benefits." For a claimant to establish that he or she "'may become eligible' for benefits, a claimant must have a colorable claim that (1) he or she will prevail in a suit for benefits, or that (2) eligibility requirements will be fulfilled in the future."

4. Examples of conflicts among the circuits on "former participant" standing:

a. *Sommers Drug Stores Co. Employee Profit Sharing Trust v. Corrigan Enters., Inc.*, 793 F.2d 1456 (5th Cir. 1986)("benefits" v. "damages").

b. *Kuntz v. Reese*, 785 F.2d 1410 (9th Cir. 1986).

c. *Harzewski v. Guidant Corp.*, 489 F.3d 799 (7th Cir. 2007).

d. *Graden v. Conexant Systems, Inc.*, 496 F.3d 291 (3d Cir. 2007).

5. Is this question technically one of "standing"? See *Harzewski*, 489 F.3d at 803-804 (issue of statutory interpretation "fundamental to the merits," as compared to statutory zone of interests standing); *Graden*, 496 F.3d at 295 ("the question presented is one of statutory standing").

6. Impact on dismissal under Fed. R. Civ. P. 12(b): narrow scope of documents that can be included to support a Rule 12(b)(6) motion to dismiss for failure to state a claim v. broader scope of documents that can be included in a Rule 12(b)(1) motion to dismiss for lack of jurisdiction. *Cf.* Amicus Brief of the Secretary of Labor, *Evans v. Akers*, No. 071-1140 (1st Cir., filed Aug. 8, 2007), at 16 n.7, urging the same result "regardless of the nomenclature."

7. Timing issues. See *Caltagirone v. NY Community Bancorp, Inc.*, 2007 WL 4467655 (2d Cir., filed Dec. 20, 2007)(no standing for participant who took a total distribution prior to the alleged fiduciary breaches); *Graden*, 496 F.3d at 296 n.7 (discussing authority under § 502(a)(1)(A) that participant status is determined "at the time of the breach," but not reaching the issue under § 502(a)(2) due to waiver).

8. Is footnote 6 in *LaRue* a precedential holding?

B. Claims under ERISA § 502(a)(3)

1. In *LaRue* the Supreme Court granted certiorari on the separate issue of whether make whole relief is available under Section 502(a)(3) of ERISA against a fiduciary. Because the Court determined that relief was available under Section 502(a)(2), it did not reach the issue of whether such relief was available under the "catch-all" provisions of Section 502(a)(3).

2. Section 502(a)(3) gives participants, beneficiaries and fiduciaries the authority to bring suit "(A) to enjoin an act or practice which violates any provision of [Title I] or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of [Title I] or the terms of the plan."

3. The Supreme Court previously held that monetary damages against non-fiduciaries do not constitute "appropriate equitable relief" in *Mertens v. Hewitt Associates*, 508 U.S. 248 (1993). Court held that in order to determine what constitutes "appropriate equitable relief" courts should return to the days of the divided bench and determine whether the relief available was typically available in equity. The Court determined that, although damages were sometimes available in equity, they were generally available in a court of law and, therefore, were not available under Section 502(a)(3).

4. An argument has been made in several cases, that make whole monetary relief against a breaching fiduciary, called surcharge during the days of the divided bench, was typically, if not exclusively, available in courts of equity and thus constitutes "appropriate equitable relief" under Section 502(a)(3).

5. This view, espoused by the Department of Labor in many of its amicus briefs, has been rejected by most courts. *See*, e.g. *Callery v. United States Life Ins. Co*., 434 F.3d 1058 (10th Cir. 2004). Justice Ginsburg in her concurring opinion in *Aetna Health Inc. v. Davila*, 542 U.S. 200, 223-24 (2004) (Ginsburg, J., concurring), however, expressed some support for that position.

6. On March 3, 2008, the Solicitor General was invited by the Supreme Court to express the federal government's views on whether certiorari should be granted in *Amschwand v. Spherion Corp.*, 505 F.3d 342 (5th Cir. 2007) which raises the same issue.

   a. Typical fact situation: After Thomas Amschwand was diagnosed with cancer, he took a leave of absence from his employer. While on medical leave, the employer switched providers for its group life insurance plan. The new policy provided that if an employee was ill and away from work on the date coverage was to be effective, coverage would be postponed until he returned to work for one day. Employer failed to tell Amschwand of the requirement, despite his numerous inquiries and he did not return to work before his death. Although he paid the premiums until his death, the insurer denied his wife's claim because Amschwand had not satisfied the active work rule. Amschwand's widow sued the employer alleging that it breached its fiduciary duties by failing to inform him of the active at work requirement and sought make whole relief in the amount of nearly $40,000, the amount she would have received had her husband been covered by the plan.

   b. Fifth Circuit affirmed the district court's decision holding that "equitable relief" in ERISA § 502(a)(3) does not include make whole relief against a breaching fiduciary. The Fifth Circuit rejected the argument that Supreme Court cases such as *Mertens* involved non-fiduciaries and were not applicable when a participant sued a fiduciary. The Court noted that other circuit courts have rejected this argument. The Court held that even though a fiduciary claim is generally an equitable claim, the remedy sought must have been one "typically" available in equity, not one that could have been brought in equity.

c. Concurring opinion notes: "The facts as detailed in Chief Judge Jones's opinion scream out for a remedy beyond the simple return of premiums. Regrettably, under existing law it is not available. I am constrained to join the court's opinion, which I find correctly applies controlling precedent."

C. Relationship to Claims and Procedures under ERISA § 502(a)(1)(B)

1. Parsing the statute – which subsection of (a)(1)(B) likely applies

2. The exhaustion requirement

3. The standard of review

a. Significance

b. Current interpretations of *Firestone v. Bruch*

4. Application to former employees and others who may not be "plan participants." Illustrative cases:

a. *Mitchell v. Emeritus Management, LLC*, 2007 WL 4212321, (D.Me.) (November 29, 2007)

b. *Todisco v. Verizon Communications, Inc.* 497 F.3d 95 (1st Cir. 2007)

5. Implications of *Met Life v. Glenn*, 461 F.3d 660 (6th Cir. 2006), *cert. granted*, 76 U.S.L.W. 3017 (U.S., Jan. 18, 2008) (No. 06-923)

6. Plaintiffs' concerns

7. Opportunities/challenges for defendants

D. Damages Theories

1. *LaRue*, 128 S.Ct. at 1024 n.4:

> The record does not reveal whether the alleged $150,000 injury represents a decline in the value of assets that DeWolff should have sold or an increase in the value of assets that DeWolff should have purchased. Contrary to respondents' argument, however, §502(a)(2) encompasses appropriate claims for "lost profits." See Brief for Respondents 12–13. Under the common law of trusts, which informs our interpretation of ERISA's fiduciary duties, see *Varity*, 516 U. S., at 496–497, trustees are "chargeable with . . . any profit which would

have accrued to the trust estate if there had been no breach of trust," including profits forgone because the trustee "fails to purchase specific property which it is his duty to purchase." 1 Restatement (Second) Trusts §205, and Comment i, §211 (1957); see also 3 A. Scott, Law on Trusts §§205, 211 (3d ed. 1967).

2. Several circuits measure a "loss" by comparing what the plan actually earned on the investment at issue with what would have been earned if the assets had been invested in other alternatives available under the plan. *E.g., Donovan v. Bierwirth*, 754 F.2d 1049 (2d Cir. 1985); *GIW Indus. v. Trevor, Stewart, Burton & Jacobsen, Inc.*, 895 F.2d, 729, 733 (11th Cir. 1990); *Dardaganis v. Grace Capital, Inc.*, 889 F.2d 1237, 1243-4 (2d Cir. 1989).

3. Some courts have compared the loss on the investment at issue with other measures of investment return as surrogates, such as prevailing interest rates or the return originally anticipated on the investment. *E.g., Katsaros v. Cody*, 744 F.2d 270, 281 (2d Cir. 1984); *Donovan v. Mazzola*, 716 F.2d 1226, 1232-33 (9th Cir. 1983).

4. Aggregation theories, where multiple breaches have resulted in both gains and losses. *E.g., California Ironworkers Field Pension Trust v. Loomis Sayles & Co.*, 259 F.3d 1036, 1047 (9th Cir. 2001) ("[the] fiduciary is liable for the total aggregate loss of all breaches" and "may be permitted to balance losses and gains attributable to multiple breaches . . .").

E. Issues for Welfare Plans

1. While *LaRue* involved a pension plan, the ruling also applies to relief sought for losses suffered by a welfare plan.

2. What constitutes "any losses" to the plan that can be recovered by Section 502(a)(2)?

   a. Losses resulting from imprudent investment of plan assets

   b. Losses from fiduciaries who engage in prohibited transactions with over-priced service providers.

   c. In *Phahler v. National Latex Co*, 2007 U.S. App. LEXIS 28886 (6th Cir. 2007) the Sixth Circuit held that participants could sue fiduciaries of a defunct plan under 502(a)(2) for losses resulting from misappropriation of employee contributions and the failure to enforce the plan's contractual claim to employer contributions necessary to pay benefit claims.

d. Losses resulting from mismanagement of pharmacy benefit programs:

(i) *Glanton v. AdvancePCP, Inc.*, 465 F.3d 1123 (9th Cir. 2006)

(ii) *Bickley v. CaremarkRX, Inc.*, 416 F.3d 1325 (11th Cir. 2006)

(iii) *Chicago Carpenters Welfare Fund v. Caremark, Inc.*, 474 F.3d 463 (7th Cir. 2007)

e. Out of pocket losses incurred by participants: *Shade v. Panhandle*¸1996 U.S. App. LEXIS 16703 (4th Cir. 1996)

f. Losses from improper use of UCR rates: *Wachtel v. Guardian Life Ins. Co.*, 2006 U.S. Dist. LEXIS 28879 (D. N.J. 2006)

g. Losses relating to MEWAs: *Chao v. Crouse*, 346 F. Supp. 2d 975 (S.D. Ind. 2004)

III. Plan Administration Practices Post-*LaRue*

A. Clarity in investment allocation procedures

1. Description of investment allocation procedures in summary plan description and prospectuses.

2. Confirm that plan administrator procedures (*e.g.*, website, 1-800 help desk) are consistent with the procedures described in the SPD.

3. QDIA disclosures and procedures.

B. Recordkeeping

1. Channeling participant communications in forms that promote recordkeeping

2. Retention of investment allocation records

C. Communications to plan participants and beneficiaries

D. Selection and monitoring of service providers

E. Plan administration procedures (SPD, etc.) that support treatment of single participant investment claims as benefits claims.