

EMPLOYEE BENEFITS ALERT

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Supreme Court Decides: 401(k) Plan Losses are Recoverable

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On February 20, 2008, the U.S. Supreme Court issued a decision in *LaRue v. DeWolff, Boberg & Associates, Inc.* that is likely to make it easier for individual participants in 401(k) plans to bring lawsuits against their employers and other plan fiduciaries for losses to their accounts arising from alleged breaches of fiduciary duty.

In the *LaRue* decision, the Supreme Court resolved a conflict between two U.S. Circuit Courts of Appeals regarding whether individual participants in a defined contribution plan may sue plan fiduciaries under ERISA for losses suffered by their accounts as a result of a breach of fiduciary duty. The Fourth Circuit Court of Appeals had ruled in *LaRue* that an individual participant in a defined contribution plan had no such right to sue under ERISA. However, the Supreme Court overturned the Fourth Circuit's decision in a unanimous opinion and held that individual participants do have the right to sue and recover losses to their individual accounts in a defined contribution plan.

The plaintiff in the *LaRue* case sued his former employer, who was the sponsor of a section 401(k) plan in which he was a participant. The plaintiff alleged that he

had directed his employer to make certain changes to the investments in his account under the plan but that his employer never carried out those directions. He claimed that this omission depleted his interest in the plan by approximately \$150,000 and that it was a breach of fiduciary duty under ERISA. The U.S. District Court granted the employer's motion to dismiss, which was upheld by the Fourth Circuit. The Fourth Circuit cited as authority for its decision a 1985 U.S. Supreme Court case known as *Massachusetts Mutual Life Insurance Company v. Russell*, which held that relief for a breach of fiduciary duty claim could only be granted for an entire plan rather than for individual participants under a plan.

In *LaRue*, the Supreme Court confined its holding in *Russell* to being applicable only to defined benefit type of plans in which participants do not maintain separate accounts within the plan. The Court said that *Russell* was aimed at protecting defined benefit plans from fiduciary misconduct that would impact the benefits that participants are entitled to receive under such plans. The Court said that the landscape of employee benefit plans has dramatically changed since *Russell* was decided in 1985. The

Court further noted that when ERISA was enacted in 1974 and when *Russell* was decided, the defined benefit plan was the “norm of American pension practice,” whereas defined contribution plans dominate the retirement plan scene today. In light of these circumstances, the Court held that ERISA does authorize recovery for fiduciary breaches that impair the value of plan assets in a participant’s individual account in a defined contribution plan.

In a concurring opinion in *LaRue*, Chief Justice Roberts strongly suggested that the appropriate recourse for the plaintiff would have been a claim for benefits under ERISA rather than a claim for breach of fiduciary duty. He stated in his opinion that if relief were available under ERISA for a claim for benefits, it is not at all clear that relief would also be available under ERISA for a breach of fiduciary duty claim by an individual plan participant. Justice Roberts stated that one of the consequences of this distinction would be that if a claim must proceed under ERISA as a claim for benefits, the participant may be required to exhaust administrative remedies before filing a lawsuit. Justice Roberts’ views in his concurring opinion may be a road map for a defense to a breach of fiduciary duty claim that is brought by an individual participant in a defined contribution plan.

What Should Plan Fiduciaries Do in Light of the *LaRue* Decision?

The *LaRue* decision eliminates a potential impediment to lawsuits under ERISA against 401(k) plan sponsors and

other plan fiduciaries by individual participants in such plans, thereby making it easier for them to obtain relief for their accounts if they are able to establish that such losses were due to a breach of fiduciary duty. Under ERISA, fiduciaries to a plan are personally liable for losses resulting from a breach of fiduciary duty. Therefore, in light of the *LaRue* decision, plan sponsors of 401(k) plans should consider taking immediate action to reduce their potential liability for such claims, including, but not limited to:

- hiring independent investment advisers to select and monitor the investment options that are chosen as investment alternatives under the plan;
- if company stock is an investment option under the plan, imposing significant limitations on the amount or the percentage of their accounts that participants can invest in such stock;
- obtaining appropriate fiduciary insurance coverage to protect plan fiduciaries from claims for breaches of fiduciary duty;
- hiring professional advisors and/or legal counsel to perform an ERISA fiduciary compliance audit of the plan; and
- complying with all the requirements of Section 404(c) of ERISA, which insulates plan fiduciaries from liability for losses resulting from a participant’s exercise of control over the investment assets in his or her account.



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For further information about the *LaRue* decision or steps that should be taken by plan fiduciaries to protect themselves from potential liability in light of *LaRue*, please contact John J. Hunter (at 215.564.8072 or jhunter@stradley.com) or James F. Podheiser (at 215.564.8111 or jpodheiser@stradley.com).



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