

## The Supreme Court's Decision in *LaRue v. DeWolff, Boberg & Associates*: How It Affects You, What You Should Do, and Ruminations Regarding the Fractured Opinion

By Joe Faucher and Mike Vanic

By now, it's likely that you have read about the decision by the United States Supreme Court in *LaRue v. DeWolff, Boberg & Associates*. Numerous newsletters and articles have commented on the Court's holding. The goal of this bulletin is to share our thoughts on what the decision means for plan sponsors and fiduciaries. At the end of the Bulletin, we offer our recommendations for plan sponsors, as well as some of our personal insights, and those of our colleagues, regarding the decision.

To understand *LaRue*, it helps to know a bit about the law as it existed before the Court's decision. The leading case in the area was another Supreme Court decision — *Massachusetts Mutual Life Ins. Co. v. Russell*. Although many commentators have suggested that *Russell* involved a defined benefit pension plan, in fact the case involved a claim for benefits under an employer-sponsored *disability* plan. When the plan fiduciaries delayed paying her claim, the plaintiff claimed that they breached their fiduciary duties under ERISA, and that she sustained damages as a result, above and beyond the benefits owed to her by the plan. The Supreme Court held that ERISA's provision authorizing the recovery of money damages by the plan, §502(a)(2), was limited to recovery of damages *by the plan*. Therefore, since the Supreme Court's 1985 decision in *Russell*, individual participants who claim to have suffered a loss due to a breach of fiduciary duty have often faced an uphill battle. If a participant sought money damages, but those money damages were not recoverable on behalf of the plan "as a whole," the participant often had no available remedy. (The classic case where money damages *were* recoverable was in the context of a plan fiduciary who failed to prudently invest defined benefit plan assets. In that type of case, alleged losses were incurred by the plan "as a whole," and the responsible fiduciaries were personally liable to pay to the plan the damages incurred.)

Thereafter, in the context of individual account defined contribution plans, some courts interpreted *Russell* to mean that if a fiduciary breach harmed an individual participant's account, but did not damage the entire plan, money damages were not recoverable. Other courts reasoned that, if a fiduciary breach damaged one or some, but not all, plan accounts, a fiduciary could be liable to the plan, and any monies recovered by the plan would be allocated to the accounts of the affected participants.

In *LaRue*, the plaintiff, James LaRue, claimed that he directed his former employer — the plan administrator — to change the investments in his 401(k) account, that the administrator failed to carry out the directive, and that as a result, he suffered a loss of approximately \$150,000. (It is unclear whether Mr. LaRue claimed that the investments in which his account had been invested lost that amount of value, or if he would have earned additional returns had the new investment instructions been carried out.) *LaRue's* facts are unusual, since the vast majority of 401(k) plan participant investment instructions are communicated via "800 numbers" or the internet directly to the investment provider, whereas Mr. LaRue alleges that he gave the investment directions to his employer.

Having lost at the trial level court, LaRue appealed to the Fourth Circuit Court of Appeals. The Court of Appeals, however, held that money damages are not available under ERISA when the claim is that only the account of an individual participant, or subset of participants, has been damaged, since the recovery in such a case would not be for the benefit of the plan "as a whole."

All of the Supreme Court Justices concluded that the Fourth Circuit Court of Appeals got it wrong. In an opinion by Justice Stevens, five of those Justices — the majority — focused their decision on the fact that individual account defined contribution plans, rather than defined benefit plans, are now the dominant form of retirement plan in the workplace. In that setting, as observed by Justice Stevens, "... fiduciary misconduct need not threaten the solvency of the entire plan to reduce benefits below the amount that participants would otherwise receive." Consequently, the decision paves the way for individual participants and beneficiaries to sue plan fiduciaries for money damages when only individual participants — or groups of participants — are adversely affected by claimed breaches of fiduciary duty. (As an aside, the *LaRue* case itself is not over. As to that case, the decision only holds that, if the plaintiff can prove the facts that he has alleged, he has a viable legal claim. There has been no decision, for instance, that his investment instructions were not properly carried out.)

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What does this mean for sponsors and fiduciaries of retirement plans, and what should they do as a result?

It is premature to predict – as some have – that *LaRue* will trigger a significant increase in ERISA litigation. The decision in *LaRue* removes one of the legal hurdles that, in some circuits (*i.e.*, parts of the country), would have dissuaded would-be plaintiffs' attorneys from taking cases in which an individual participant, or small group of participants, have sustained damage to their plan accounts. While that legal hurdle has been removed, other practical issues will be the deciding factors for plan participants contemplating litigation. A threshold issue for any plan participant is whether the amount of their claimed losses due to a fiduciary's breach is significant enough to justify litigation. And, as mentioned above, even before the Supreme Court's decision in *LaRue*, Circuit Courts of Appeals in other parts of the country had already held that individual participants could sue to recover damages that occurred as the result of a breach of fiduciary duty that impacted only their own plan account, yet the courts in those circuits experienced no significant increases in ERISA litigation.

That said, the case will focus yet more scrutiny on ERISA fiduciaries, and plaintiffs' attorneys will point to the decision as a sign that previous legal hurdles to their claims no longer exist. Consequently, the first and easiest thing that plan sponsors and fiduciaries should do is to be sure that their liability insurance coverage covers them in the event of such a claim.

The *LaRue* decision also presents some meaningful issues for employers to consider in operating their plans. For example:

- Communications with plan participants should clearly state who is – and who is not — responsible for carrying out participant and beneficiary investment instructions. Those documents should clearly state that participants should communicate investment instructions directly to the plan's investment providers.
- When plan administrators become aware of an error on the part of an investment provider or service provider that results in damage to a participant's account, they may be obligated to demand that the company that made the error take action, at the investment provider or service provider's expense, to rectify the error. Therefore, it is imperative that plan sponsors carefully review their contracts with investment providers. Do those contracts purport to relieve the provider of any wrongdoing in failing to carry out participant investment instructions? If so, plan fiduciaries should consider negotiating with the provider to eliminate any such terms, or obtaining some benefit to the plan for allowing the term to remain in the provider's contract. The employer should carefully document this process.

Moreover, everyone involved in 401(k) plan administration – employers, fiduciaries, third party administrators and investment providers — should review their agreements with the others involved in the process. Do the agreements clearly spell out who is responsible for carrying out participant investment instructions?

Those documents should be consistent with the plan, and with the summary plan description.

### How We See *LaRue*

Again, it's too soon to say that *LaRue* will result in a significant expansion of ERISA litigation, but the decision is certain to have an impact on the world of employee benefits in general, and ERISA litigation in particular. To understand why, you need to know a bit more about the Court's opinion. Although all nine Justices of the Supreme Court agreed with the outcome, there was some divergence in the path they took to that outcome. The result is that the Court actually issued *three* opinions – the majority opinion (discussed above), and two opinions concurring in the judgment.

In the first of these concurring opinions, Chief Justice Roberts, joined by Justice Kennedy, wrote that, while he agreed that the analysis of the Fourth Circuit Court of Appeals was "flawed," it is not clear that *LaRue* brought his claim under the correct provision of ERISA. Specifically, Chief Justice Roberts concluded that "[i]t is at least arguable that a claim of this nature properly lies only under [ERISA's provision allowing participants and beneficiaries to pursue claims for benefits]," rather than the provision that allows a claim for damages to the plan as a result of a fiduciary breach.

In the second of *LaRue*'s two concurring opinions, Justice Thomas, joined by Justice Scalia, wrote that whether a claim is available to *LaRue* does not depend on "trends in the pension plan market" (*i.e.*, the trend away from defined benefit plans to defined contribution plans). Rather, according to Justice Thomas, the losses to *LaRue*'s individual account resulting from purported breaches of fiduciary duty were losses of "plan assets," which, once recovered, were simply attributable to Mr. *LaRue*'s individual account: "... when a defined contribution plan sustains losses, those losses are reflected in the balances in the plan accounts of the affected participants, and a recovery of those losses would be allocated to one or more individual accounts."

These three opinions represent three distinct philosophical approaches to the same problem. The majority opinion suggests that it represents a shift in the law that coincides with the shift from the widespread use of defined benefit plans, to the widespread use of defined contribution (401(k)) plans.

To the extent it is relied upon by future courts, the Roberts opinion suggests that claims of this nature should not even be decided under ERISA's fiduciary breach provisions, but rather, should be approached as a claim for benefits. That notion, if followed by the lower courts, would arguably favor plan administrators, that is, plan sponsors and fiduciaries.

Our own observations on these divergent opinions follow:

**Mike Vanic:** The concurring opinion by Chief Justice Roberts is inconsistent with traditional ERISA notions. First, it's difficult to understand how one could characterize a claim like *LaRue* as a claim for plan benefits. After all, Mr. *LaRue* wasn't looking for a distribution of the assets in his plan account, and in fact, he appears to have received a full distribution of his plan benefits prior

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to the Supreme Court's decision. What he was arguing was that his plan benefits would have been greater but for the fiduciary's breach. The cases consistently hold that only the plan itself is liable to pay the benefits owed to the participant. The plan could not pay *LaRue* additional benefits from plan assets – from which participants should they be taken? Thus, he was properly looking for the *fiduciaries* – who are potentially personally responsible for breaches of fiduciary duty – to deposit additional amounts into his plan account, thereby increasing his account and benefits. Without the infusion of additional funds into his account from a source other than the plan, he had no additional plan benefit to be distributed to him.

Second, benefit claims under ERISA are subject to an entire distinct body of law, which typically requires participants to first exhaust the administrative remedies provided for by the plan before filing a lawsuit. In most cases, that means submitting a claim to the plan administrator or administrative committee to decide whether benefits, or additional benefits, are owed by the plan. If the plan provides that the administrator has discretion to interpret the terms of the plan, and to decide whether benefits are payable, a court reviewing the administrator's decision will often give deference to that decision unless it finds that the administrator abused its discretion in coming to its decision. Most circuits that have considered the issue have rejected the concept of requiring the participants to exhaust administrative claim procedures prior to filing an action for breach of fiduciary duty. In many cases, that would result in the very same allegedly breaching fiduciary being in control of the administrative review process.

**Joe Faucher:** *LaRue* may give plaintiffs' attorneys an opportunity to argue that other fundamental changes in the law are necessary now that the retirement plan landscape is dominated by defined contribution plans, rather than defined benefit plans. As Justice Thomas's concurring opinion points out, *LaRue* could easily

have been decided based on the very narrow basis that a breach of fiduciary duty may result in damage to the plan, even if the recovery is allocated to the account of some but not all participants. Instead, the majority of the Justices rested their opinion in part on the idea that "*Russell's* emphasis on protecting the 'entire plan' from fiduciary misconduct reflects the former landscape of employee benefits. That landscape has changed." Thus, the majority of the Supreme Court has concluded that a change in the retirement plan marketplace warrants a change in the way the law should apply. Ironically, the *Russell* case did not involve a retirement plan *at all* — it involved a disability benefit plan.

**Fred Reish:** I believe Justices Thomas and Scalia got it right. If the fiduciaries of a 401(k) plan breach their duties, and a loss results, the plan suffered a loss . . . regardless of whether the loss (and any litigation recovery) is allocated to one participant's account, to some of the accounts, or to all of the accounts. However, I do not believe this will result in a tsunami wave of fiduciary breach litigation—because that would require a tsunami of fiduciary breaches, which is not happening. In my experience, most plan sponsors, and their officers and committee members, are being attentive to their duties and fulfilling their legal responsibilities.

**Debra Davis:** The *LaRue* decision created consistency among the courts and the guidance issued by the U.S. Department of Labor (the "Department"). The Department and numerous courts have interpreted ERISA as requiring fiduciaries to use a prudent process when making decisions with respect to their plans. That is, fiduciaries need to gather the relevant information and then make decisions based on that information. The significant standards imposed on fiduciaries would lack meaning if fiduciaries were not responsible for the failure to act in accordance with those standards. As a result, *LaRue* is a reminder to fiduciaries that ERISA's requirements apply regardless of the number of participants that are impacted.

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