THE SUPREME COURT SAYS PARTICIPANTS CAN SUE YOU

LARUE v. DEWOLFF, BOBERG & ASSOCIATES, INC.

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Introduction

Last month, in *LaRue v. DeWolff, Boberg & Associates, Inc.*, No. 06 Civ. 856, the U.S. Supreme Court ruled that ERISA permits a participant in a defined contribution plan to bring an action to recover the losses attributable to his/her account that were caused by a fiduciary breach. Prior to this ruling, the lower courts were divided on whether certain Sections of ERISA provide remedies for entire plans, or for individuals as well.

This letter provides background to the case and summarizes the Court's finding. As a reminder, we are not attorneys. We are investment consultants and fiduciaries to our clients' plans, and our treatment of this case is meant to answer the basic questions clients have been asking us, among which are, does this case matter to us? Does it provoke a wave of participant lawsuits for breach of fiduciary duty? Are we at risk?

For the most part, our answer is no. We do not feel are clients are at any greater risk than prior to the ruling. Clients of most every size have administrative claims processes in place that would have adequately addressed the issues involved in the suit. Further, the concurring opinion of Chief Justice Roberts recognized that allowing a 502(a)(1)(B) benefit claims action to be recast as a Section 502(a)(2) fiduciary breach might permit plaintiffs to circumvent the evidentiary and procedural processes that already exist – and that the appropriate relief (a fiduciary breach or benefit claim) still needs to be decided by the lower courts in this particular case.

What this means is the Supreme Court did not rule on the merits of the LaRue case; the case was sent back to the lower courts for judgment. Instead the Supreme Court ruled on an issue that has been dividing the courts, finding that the current retirement landscape with a strong weight of 401(k) programs makes it necessary to rethink the legal interpretation of "plan assets" and allow for asset recovery to individual accounts.

OUR TREATMENT OF THIS CASE IS MEANT TO ANSWER THE BASIC QUESTIONS OUR CLIENTS HAVE BEEN ASKING US.

Our summary of the case and finding follows.

Background

Mr. James LaRue filed an action in 2004 against his former employer, DeWolff, Boberg & Associates (DeWolff), and the ERISA-regulated 401(k) retirement savings plan administered by DeWolff. Mr. LaRue alleged that in 2001 and 2002 he directed DeWolff to make certain changes to the investments in his individual account, but DeWolff never carried out these instructions. Mr. LaRue claimed that this omission "depleted" his interest in the Plan by approximately $150,000, and amounted to a breach of fiduciary duty under ERISA. From public 5500 filings we can ascertain that the Boberg & Associates Employees Savings Plan had about 150 participants and assets of $3.7 million at the end of 2001.

On June 23, 2005, a federal district court in South Carolina granted Mr. LaRue's motion for a judgment on the pleadings. On appeal, the Fourth Circuit Court ruled against him, indicating Section 502(a) is restricted by its terms to actions invoking fiduciary liability under Section 409(a), and Section 409(a) provides for recovery by the Plan, not the participant or beneficiary who brings suit. The judgment relied on the Supreme Court's 1985 decision in *Massachusetts Mutual Life Insurance Company v. Russell,* which provided for a recovery that would inure to a pension plan as a whole and not for a recovery for an individual participant.

THE SUPREME COURT UNANIMOUSLY HELD THAT ERISA SECTION 502(a)(2) DOES AUTHORIZE RECOVERY FOR FIDUCIARY BREACHES.

The key questions raised in by Mr. LaRue's petition to the Supreme Court were:

- Does Section 502(a)(2) of ERISA permit a participant to bring an action to recover losses attributable to a participant's account in a "defined contribution plan" that were caused by fiduciary breach?
- Does Section 502(a)(2) of ERISA permit a participant to bring an action for monetary "make-whole" relief to compensate for losses directly caused by fiduciary breach?

Supreme Court Finding

On February 20, 2008, in an opinion authored by Justice Stevens, the Supreme Court unanimously held that ERISA Section 502(a)(2) does authorize recovery for fiduciary breaches that impair the value of plan assets in a participant's individual account.

Justice Stevens (who wrote the decision in Russell) stated that the "entire plan" was a sensible application of Section 409 and Section 502(a)(2) in the historical context of defined benefit plans, but that the subsequent proliferation of defined contribution plans has rendered the Massachusetts Mutual Life Insurance Company v. Russell decision inapplicable. The Court found that a breach of fiduciary duty that harms a single participant creates the kind of harm that concerned the draftsmen of Section 409, writing:

Section 502(a)(2) provides for suits to enforce the liability-creating provisions of Section 409, concerning breaches of fiduciary duties that harm plans. The Court of Appeals cited language from our opinion in Russell suggesting that these provisions "protect the entire plan, rather than the rights of an individual beneficiary." It then characterized the remedy sought by petitioner as "personal" because he "desires recovery to be paid into his Plan account, an instrument that exists specifically for his benefit".

As the case comes to us we must assume that the respondents breached fiduciary obligations defined in Section 409(a), and that those breaches had an adverse impact on the value of the plan assets in the petitioner's individual account. Whether petitioner can prove those allegations and whether respondents may have valid defenses to the claim are matters not before us.

Opinion of Chief Justice Roberts

Chief Justice John G. Roberts issued a concurring opinion that has sparked some interest among ERISA lawyers. He writes that although the Court concludes Section 502(a)(2) does authorize recovery in cases such as *LaRue v. DeWolff, Boberg & Associates, Inc.,* the Court did not consider whether relief under Section 502(a)(1) was more appropriate. The Court had no occasion to address that argument, as Mr. LaRue brought his claim under Section 502(a)(2).

Chief Justice Roberts goes on to write that LaRue's claim is a claim for benefits that turns on the application and interpretation of the Plan terms, specifically those governing investment options and how to exercise them, and that it is at least arguable that a claim of that nature properly lies only under Section 502(a)(1) of ERISA. That provision allows a plan participant or beneficiary to recover benefits due to him under the terms of the Plan, to enforce his rights under the terms of the Plan, or to clarify his rights to future benefits under the terms of the Plan.

The significance of the distinction between a Section 502(a)(1) claim and one under 502(a)(2) is described as more than a matter of picking the right provision to cite in a complaint, *If LaRue may bring his claim under Section 502(a)(1)(B), it is not clear that he may do so under 502(a)(2) as well.*

Section 502(a)(2) provides for appropriate relief. Construing the same term in a parallel ERISA provision, we have held that relief is not "appropriate" under Section 502(a)(3) if another provision, such as Section 502(a)(1)(B) offers an adequate remedy.

Allowing a 502(a)(1)(B) action to be recast as one under Section 502(a)(2) might permit plaintiffs to circumvent safeguards for plan administrators that have been developed under Section 502(a)(1)(B).

BENEFIT CLAIM MATTERS SUCH AS MR. LARUE'S WILL NOT NORMALLY END UP IN THE COURTS.

Should the opinion of Chief Justice Roberts hold, we understand from ERISA lawyers that lower courts would be challenged to allow Section 502(a)(2) fiduciary breach suits because doing so would bypass the obligation to utilize the normal administrative appeal mechanisms before turning to the courts.

Opinion of Justice Thomas

Justice Clarence Thomas issued a concurring opinion that was reportedly praised by two prominent ERISA lawyers, Fred Reish of Reish Luftman Reicher & Cohen, and Mike Prame of Groom Law Group. Thomas' opinion was that the Court should have ruled in LaRue's favor simply by interpreting the language of ERISA.

Justice Thomas explained that his agreement with the majority's holding was not contingent on any trends in the pension market. Instead, ERISA requires the assets of a defined contribution plan be allocated for bookkeeping purposes to individual accounts within the plan. Any losses are reflected in the balances in the accounts of the affected participants, and a recovery of those losses would be allocated to one or more individual accounts. In essence, the allocation of a Plan's assets to individual accounts for bookkeeping purposes does not change the fact that all the assets in the Plan remain Plan assets. Therefore, Justice Thomas concludes that if a participant sustains losses to his account as a result of fiduciary breach, the Plan's aggregate assets are likewise diminished by the same amount, and Section 502(a)(2) permits the participant to recover such losses on behalf of the plan.

NEPC Comments

Our clients' concerns about ending up in court for fiduciary breach suits are not immaterial. A function of our role as Consultant and fiduciary is to help ensure that the appropriate governance and due diligence processes are in place to help our clients meet their fiduciary obligations.

In this letter we discuss the *LaRue v. DeWolff, Boberg & Associates, Inc.* case, as we've come to understand it over the past few weeks. We share the view that we have formed in concert with a half dozen ERISA attorneys that benefit claim matters such as Mr. LaRue's will not normally end up in the courts as fiduciary breach suits. There are normal evidentiary and procedural processes that deal with benefit claim matters, and safeguards to that effect for plan sponsors.

A simple take away from this case is to be reminded that fiduciaries retain liability in areas including running the Plan according to the Plan's governing documents and disclosures. While plan sponsors normally spend a great deal of time on investment related matters, this case serves as a reminder that recordkeeping and administrative excellence are also a critical component of your program's success.

Postscript: In October 2008 the case was dismissed with prejudice after LaRue withdrew his claim, indicating that it was not financially feasible for him to pursue it further.