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Alert

Change Brewing in Fiduciary Liability

Take nothing for granted. This is one clear message that emerges from a review of recent court activity related to Fiduciary Liability. Matters as basic as who can sue under the Employee Retirement Income Security Act (ERISA) and on what grounds they can sue are at play. Below we examine the current state of two key questions.

- Who has standing to bring an action under ERISA?
- Can plan fiduciaries be held liable for financial losses resulting from the failure to carry out a participant's investment instructions?

Who Can Sue?

Only a privileged few may bring suits under ERISA. These include plan fiduciaries, participants, beneficiaries and those representing the plan itself. For the 33 years since ERISA was enacted, the Fiduciary world has understood that past participants who have cashed-out and received all of their benefits under a plan may ***not*** sue. This has recently changed, at least in some courts.

Starting with an appeals court decision in New York in June, followed in quick succession by decisions in ERISA cases in Massachusetts, New Jersey and Ohio, the courts took a broader view of the rights of a cashed-out participant. These courts embraced the theory that a former participant could have standing to bring suit under ERISA if, as a result of their suit, they might become eligible to receive additional benefits from a plan.

In the New York case, *Harzewski v. Guidant Corporation*, the court concluded that to be able to sue, the plaintiffs must be able to "show that they are claiming an amount of money to which they are entitled by the plan documents over what they received when they retired and received the money in their retirement accounts." In siding with the plaintiffs, the court compared fiduciary mismanagement to theft, at least in its result, holding that "…there is no difference if instead of stealing the money from the account, Guidant by imprudent management caused the account to be half as valuable as it would have been under prudent management."

All four cases are ERISA tagalong cases – claims brought as parallel suits to securities class actions where there is (or was) company stock in the company's pension plan. The status of tagalong cases was addressed directly in the *Guidant* case. The defense argued that the plaintiffs in an ERISA tagalong action don't need an ERISA remedy as they can collect under the securities fraud suit. The court concluded that the ERISA rights would not necessarily be protected in the context of a securities case because fraud can be harder to prove in the securities context, where there is no established fiduciary relationship as exists under ERISA. Because the duty of care is higher under ERISA, the court affirmed that separate ERISA suits are justified.

The court's ruling in this case also answered a crucial insurance-related question: did the amount sought by plaintiffs constitute the receipt of a plan benefit? The court unequivocally concluded that it did. This presents potential insurance coverage concerns as the standard ERISA Fiduciary Liability policy excludes benefits due to participants. (We addressed these issues in our October 2006 *Alert* article, "What Does the Fiduciary Liability Policy Pay If It Doesn't Cover Benefits").

On What Grounds Can Participants Sue?

The Supreme Court has agreed to decide whether a 401(k) plan participant can sue to recover losses allegedly resulting from the failure to carry out the participant's investment instructions. While the financial stake in *LaRue v. DeWolff, Boberg & Associates* is a mere $150,000, the outcome will be important for ERISA fiduciaries generally. The Court

agreed to review the case in response to Department of Labor (DOL) concerns that federal circuit courts are split on the subject. The Fourth Circuit affirmed a dismissal on the grounds that failure to carry out instructions is insufficient grounds for a suit. Four other circuit courts have held that plaintiffs in similar situations have a recognizable ERISA claim for damages.

The Insurance Perspective

On the whole, these cases appear to represent an increase in exposure for those with fiduciary responsibilities. Fortunately for fiduciaries, ERISA Fiduciary Liability carriers seem to have absorbed the message of these cases and are not flinching. One leading carrier even introduced some additional policy wording to provide assurance that claims á la *Guidant* and possible resulting damages would be covered (subject to the other terms and conditions of the policy). Other major insurers have confirmed similar positions. Whether this encouraging news balances the increase in liability remains to be seen.

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