



Travelers Wrap+ Fiduciary Liability

Recent U.S. Supreme Court Decision Makes It Easier for Individual 401(k) Participants to Sue for Breach of Fiduciary Duty under ERISA

A recent decision by the U.S. Supreme Court makes the management and administration of 401(k) plans more perilous than ever before. On February 20, 2008, in the case of *LaRue v. DeWolff, Boberg & Associates, Inc.*,¹ the Court issued a unanimous decision authorizing a single 401(k) plan participant to bring suit against his former employer for allegedly failing to invest his money as he directed. Prior to the Court's decision in *LaRue*, most lower courts held that Section 502(a)(2) of ERISA, which governs suits for breach of fiduciary duty, only authorizes suits by individual plaintiffs so long as such suit was on behalf of the plan itself or on behalf of a class of similarly situated plaintiffs.

Essentially, the effect of those lower court holdings was that a plan participant had no legal recourse to remedy a fiduciary breach, unless the alleged breach affected multiple plan participants or the plan as a whole. However, as a result of the Court's decision in *LaRue*, a breach of fiduciary duty that causes a loss to just one 401(k) individual investment account may be actionable under ERISA. Therefore, fiduciaries of 401(k) plans, and possibly other types of pension plans, now face an even greater risk of being sued for breach of fiduciary duty.

> Whose Liability Exposure Has Changed As a Result of *LaRue*?

LaRue increases the liability exposure of plan fiduciaries. ERISA's definition of "fiduciary" is expansive. This broad definition includes any person or entity that:

- is designated as a named fiduciary in a plan instrument;
- exercises any discretionary authority or control respecting management of a plan or disposition of its assets;
- has discretionary authority or responsibility in the administration of a plan; or
- renders investment advice for a fee with respect to plan assets.

Further, it is not uncommon for plaintiffs involved in ERISA litigation to allege that a plan's trustee, administrator, and sponsor and the sponsor's board of directors, senior officers and certain employees are all ERISA fiduciaries.



¹ 128 S. Ct. 1020 (2008).

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> What Are the Liability Exposures of ERISA Plan Fiduciaries?

The principal obligations of ERISA plan fiduciaries that give rise to potential fiduciary liability relate to the proper management, administration, and investment of fund assets, the maintenance of records, the disclosure of specified information, and the avoidance of conflicts of interest. Among those obligations are the overlapping statutory fiduciary duties set forth in ERISA that require plan fiduciaries to:

- (1) Act solely in the interest of the participants and beneficiaries for the exclusive purpose of:
 - (i) Providing benefits to participants and their beneficiaries; and
 - (ii) Defraying reasonable expenses of administering the plan;
- (2) Act with the care, skill, prudence and diligence under the circumstances that a prudent person acting in a like capacity and familiar with such matters would use;
- (3) Diversify the plan's investments to minimize the risk of loss unless, under the circumstances, it is clearly prudent not to diversify; and
- (4) Follow the documents and instruments governing the plan to the extent that they are consistent with ERISA.

ERISA provides that any plan fiduciary that breaches any of the above duties shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary. Additionally, ERISA authorizes the assessment of statutory penalties and the award of attorney fees in certain situations.

According to the Tillinghast 2003 Fiduciary Liability Survey Report, the average fiduciary liability claim payment was \$994,000. The same study reported that the average cost to defend a fiduciary liability lawsuit was approximately \$365,000. The burden of proof for compliance with all provisions of ERISA lies with the sponsor/employer. With average attorney fees of \$250/hour, even meritless allegations will be costly to defend.

> Think ERISA Section 404(c) Eliminates a Fiduciary's Personal Liability Associated with 401(k) Plans? Think again!

401(k) plans continue to grow in popularity. Most employers and individual fiduciaries are under the belief that their fiduciary liability has been completely eliminated by providing a 401(k) plan which complies with ERISA section 404(c). While Section 404(c) may reduce a fiduciary's liability for investment losses that result from a participant's exercise of control over assets in his or her individual 401(k) investment account, a fiduciary's failure to comply with just one of the 20 – 25 conditions in section 404(c) may nullify such protection. According to some experts, very few plans actually comply with section 404(c). Additionally, be aware, important responsibilities and potential liabilities cannot be transferred.

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Under ERISA section 404(c) a sponsor is still required to:

- Provide sufficient information and education so participants can make informed decisions
- Provide at least three core investment alternatives
- Offer investment alternatives with various levels of risk
- Select competent investment managers
- Routinely monitor and evaluate investment performance
- Control costs, which are in most cases, borne by the participants
- Provide a mechanism for self-direction of participant's investments

> **Fiduciary Liability Coverage from Bond & Financial Products is the Solution**

Bond & Financial Products' Fiduciary Liability policy covers fiduciaries of employee benefit plans for defense expenses and sums they are legally obligated to pay as a result of an actual or alleged "wrongful act" or breach of their fiduciary duties. The plans themselves and the plan sponsor are also covered. Travelers was the first to develop fiduciary liability coverage to meet the changing needs of employee benefit plan fiduciaries in 1974. Our Fiduciary Liability insurance combines that experience with state of the art coverage and expert claims handling.

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