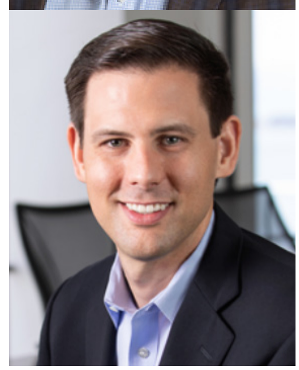
TRUCKER ✦ HUSS

U.S. Supreme Court Considering Three ERISA Cases in October Term 2019



JOSEPH C. FAUCHER
and BRIAN D. MURRAY

NOVEMBER, 2019

The Employee Retirement Income Security Act of 1974 (ERISA) has generated numerous U.S. Supreme Court decisions since its enactment, and this year's term is no exception. The Court is currently considering three ERISA cases involving a range of significant issues.

First, in *Retirement Plans Committee of IBM v. Jander*, the Court will reexamine the pleading standard plaintiffs must satisfy in order to avoid dismissal of lawsuits alleging that a fiduciary failed to prudently act on inside information in managing plans that offer company stock (commonly known as "stock drop" cases). Second, in *Intel Corp. Inv. Policy Comm. v. Sulyma*, the Court will decide whether ERISA's three-year statute of limitations, which runs from the earliest date on which a plaintiff has "actual knowledge" of a fiduciary breach, bars suit where a plaintiff has access to all relevant information more than three years prior to filing the lawsuit, even if he or she failed to actually review the information. Third, in *Thole v. U.S. Bank, N.A.*, the Court will consider whether a participant in an ERISA-governed defined benefit pension plan may sue to restore losses to the plan caused by a fiduciary breach, even if the plan is capable of paying all benefits due. We address each of these cases below.

Retirement Plans Committee of *IBM v. Jander*[1]

The Supreme Court's decision in *Fifth Third Bancorp v. Dudenhoeffer*, 134 S.Ct. 2459 (2014), made it very difficult for plaintiffs to survive early motions to dismiss in cases challenging the inclusion of the sponsor company's stock as a plan investment option. In these so-called "stock drop" lawsuits, which were common prior to *Dudenhoeffer*, plaintiffs typically allege that fiduciaries failed to prudently: (i) sell the plan's holdings in the company stock, (ii) cease additional purchases of the stock, or (iii) disclose negative inside information to the market.

Dudenhoeffer requires plaintiffs to satisfy a rigorous two-part test in order to successfully allege that a fiduciary failed to prudently act on non-public information in managing plans that offer company stock. First, plaintiffs must sufficiently plead an alternative action the fiduciary could have taken that would not have violated securities laws (i.e., insider trading rules). Second, plaintiffs must plead facts that show why a prudent fiduciary in that fiduciary's position would not have viewed the alternative action as more likely to harm the stock fund than help it.

In the wake of *Dudenhoeffer*, courts across the country have dismissed almost every "stock drop" lawsuit under this two-part test. However, the U.S. Court of Appeals for the Second Circuit reversed that trend in *Jander v. Ret. Plans Comm. of IBM, 910 F.3d 620 (2d Cir. 2018).*

The plaintiffs in Jander were participants in a 401(k) plan sponsored by IBM. One of the Plan's investment options was an IBM Company Stock Fund (the "Fund"), which was primarily invested in IBM stock. In October 2014, IBM announced the sale of its microelectronics business division, and a related $2.4 billion write-down of its assets, which caused IBM's share value to decline by over 7%. The plaintiffs alleged that IBM knew this division was struggling financially, but failed to take action to prevent the foreseeable drop in IBM's stock price that occurred once IBM announced the sale of the division.

The plaintiffs claimed that IBM could have taken several alternative courses of conduct to mitigate the losses to the Fund, including making earlier public disclosures about the true financial health of the microelectronics division, which in turn would have reduced IBM stock to its actual value. The district court dismissed the case under *Dudenhoeffer* on the grounds that the plaintiffs failed to allege that a prudent fiduciary in the defendants' position would not have viewed their proposed alternatives as more likely to harm the Fund than help it. Other district courts had previously rejected the "earlier disclosure" theory advanced by the *Jander* plaintiffs.

On appeal, the Second Circuit reversed, concluding that "several allegations" in the plaintiffs' complaint stated a viable claim under *Dudenhoeffer*. First, it found the plaintiffs sufficiently pled that the Plan's fiduciaries knew the IBM stock was artificially inflated because they knew about the microelectronics division's struggles. Second, it found the fiduciaries could have disclosed information about the division's actual financial health earlier through IBM's quarterly SEC filings and normal participant disclosures. Third, it found that Plan fiduciaries could have foreseen that an inevitable disclosure of the division's financial struggles would have negative effects on IBM's reputation and value. Fourth, a reasonable fiduciary would not have feared the market would overreact to an early disclosure, because IBM traded in an efficient market, and a truthful disclosure would bring the stock to its true value. Fifth, the court concluded that fiduciaries knew that disclosure about the struggling division was inevitable because they were actively working to sell it. The court found this fifth point "particularly important" because this was not a case where the decision was to release the information or not to release it. Rather, it was a decision between an early disclosure and an inevitable later disclosure.

The Supreme Court agreed to hear argument on whether *Dudenhoeffer*'s "more harm than good" pleading standard can be satisfied by generalized allegations that an earlier disclosure would have benefited the plan. The Court heard oral argument earlier this month, but has not yet issued a decision. Corporate insiders who also serve as plan fiduciaries will be paying close attention to the *Jander* decision, which may provide clearer guidance as to how such insiders should conduct themselves to balance their fiduciary duties under ERISA with their duties as insiders under the securities laws.

Intel Corp. Inv. Policy Comm. v. Sulyma

ERISA's statute of limitations requires plaintiffs to bring claims for breach of fiduciary duty within three years of the date on which they have "actual knowledge" of the breach or violation. *Intel Corp. Inv. Policy Comm. v. Sulyma* presents the Supreme Court with an opportunity to address the meaning of "actual knowledge," which is currently the subject of directly conflicting decisions in the Sixth and Ninth Circuits.

In *Sulyma*, a former employee and participant in two of Intel's retirement plans, brought a putative class action against the plans' fiduciaries, alleging that they committed fiduciary breaches by imprudently investing the plans' assets in two funds, which underperformed following the Great Recession relative to index funds and comparable portfolios due to higher fees and unduly risky investment choices.

Sulyma alleged that upon learning about the funds' poor performance, he filed his complaint against Intel on October 29, 2015 in the U.S. District Court for the Northern District of California. Intel moved to dismiss Sulyma's complaint as time-barred, on the grounds that Sulyma had actual knowledge of the alleged breach more than three years before filing the complaint.

Intel pointed to the fact that it had disclosed information about the plans' asset allocation and underlying investment strategy more than three years prior to the filing of the complaint. Specifically, Intel pointed to various documents it made available to Sulyma and all other plan participants, and several disclosures on Intel websites explaining Intel's investment choices. Sulyma accessed some of this information on Intel's websites, but testified that he was not actually aware of the precise composition of his retirement accounts. The district court dismissed the case as time-barred under the three-year statute of limitations, and Sulyma appealed.

The Ninth Circuit reversed, holding that Sulyma did not have "actual knowledge" of Intel's alleged breaches more than three years before filing his lawsuit. The court held that "actual knowledge" means something between "bare knowledge of the underlying transactions" and actual knowledge of the existence of a claim under ERISA. The court explained that in order to invoke the three-year statute of limitations, a defendant must show that the plaintiff has "sufficient knowledge to be alerted to the particular claim" under ERISA. The court concluded that although Sulyma had sufficient information available to him to know about the allegedly imprudent investments more than three years before he filed suit, a dispute of fact existed as to whether he had "actual knowledge" based on his deposition testimony that he was unaware that the funds had been invested in risky investments, and that he did not recall reading the documents alerting him to such investments.

Sulyma directly contradicts the Sixth Circuit's decision in *Brown v. Owens Corning Investment Review Committee*, 622 F.3d 564 (6th Cir. 2010). The court in that case held that when a plan participant is given specific instructions on how to access plan documents, his failure to read the documents does not shield him from having actual knowledge of the documents' terms. On June 10, 2019, the Supreme Court agreed to hear argument regarding the meaning of "actual knowledge." Oral argument is scheduled for December 4, 2019.

Thole v. U.S. Bank, N.A.

In *Thole*, two participants in the U.S. Bank defined benefit pension plan brought a putative class action against the plan's fiduciaries, alleging that they breached their fiduciary duties and engaged in prohibited transactions under ERISA by investing the Plan's entire investment portfolio in equities, including over 40 percent of the Plan's assets in parent company U.S. Bancorp's own mutual funds.

The plaintiffs alleged that the defendants' investment decisions resulted in the Plan suffering losses of $1.1 billion in 2008, thereby causing the Plan to go from being significantly overfunded in 2007 to being underfunded in 2008, where it remained through the filing of the lawsuit in 2013. The plaintiffs alleged that the Plan would have suffered smaller losses in 2008 had the defendants properly diversified Plan's assets. The defendants moved to dismiss the complaint arguing, among other things, that the plaintiffs lacked standing to sue, because they could not establish that they had suffered any individual losses. This is a common argument in cases involving defined benefit plans, where the plan sponsor essentially bears the risk of underfunding. The district court determined that although the plaintiffs did not allege that their benefit levels had actually decreased, they had standing to pursue their claims because defendants' alleged breaches injured the plaintiffs by causing an increased risk of default to the Plan.

While the lawsuit was pending, defendants made $311 million in voluntary excess contributions to the Plan, thereby causing the plan to once again become overfunded. The defendants then moved to dismiss the plaintiffs' lawsuit on the basis that the plaintiffs no longer had standing to sue. The district court dismissed the case, but did so on the basis that the case became moot once the plan was overfunded. Thus, the court reasoned, the plaintiffs no longer had a concrete interest in the monetary and equitable relief they originally sought.

On appeal, the U.S. Court of Appeals for the Eighth Circuit affirmed the district court's dismissal of the plaintiffs' lawsuit on the basis that the plaintiffs lacked statutory standing under ERISA. The court held that in order to bring suit for fiduciary breach under ERISA sections 502(a)(2) and (a)(3), plaintiffs must show actual injury) — to the plaintiffs' interest in the plan under (a)(2) and to the plan itself under (a)(3) — and that no injury exists where the plan is overfunded. In so ruling, the Eighth Circuit broke from the Second, Third and Sixth Circuits, which have held that no individual financial loss is necessary to seek injunctive relief under ERISA §502(a)(3).

The Supreme Court agreed to hear arguments regarding whether an ERISA plan participant or beneficiary may seek monetary or injunctive relief under ERISA § 502(a)(2) and (3) without demonstrating individual financial loss or the imminent risk thereof, and whether the plaintiffs have demonstrated Article III standing. Oral argument is scheduled for January 13, 2020.

The *Thole* decision will have significant implications for defined benefit plan fiduciaries. Should the Supreme Court affirm the Eighth Circuit's decision, it will provide defendants in defined benefit plan fiduciary breach litigation with a powerful tool to obtain dismissal of lawsuits alleging fidciary misconduct, so long as the plan remains fully funded and able to pay out benefits to retirees.

———————

[1] For further discussion regarding this case, see Joseph C. Faucher and Dylan D. Rudolph, "Second Circuit Breathes New Life Into Company Stock Litigation," Trucker Huss Benefits Report Newsletter, February 2019 (Vol. 28, No. 2).

EMAIL JOSEPH FAUCHER