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Emerging Theories of Liability in ERISA Litigation and Lessons Learned for Plan Fiduciaries

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Overview

- Participant Data Claims
- Fraud and Cybersecurity
- Lessons Learned & Fiduciary Best Practices

Participant Data Claims

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Participant Data Claims

- What are plaintiffs referring to as participant data?
  - Participant names and contact information,
  - Social security numbers and dates of birth,
  - Phone numbers, work and personal email addresses,
  - Income levels, expected retirement age, marital status,
  - Investment histories, investment holdings, investment contribution amounts and account balances.

- Plaintiffs allege this data is it being used to:
  - Cross-sell non-plan products such as IRAs, high interest credit cards, life insurance, banking products, advisory accounts, individual brokerage accounts, and options trading accounts.

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Participant Data Claims

- Emerging claims are based on alleged misuse of participant data and are premised on allegations that a participant's personal data is property and a plan asset.
- If participant data is a plan asset, plaintiffs allege that the data is subject to ERISA's prohibition that plan assets cannot be used for the benefit of parties-in-interest.
- Plaintiffs claim that fiduciaries breach their duties and allow prohibited transactions when they do not prevent plan service providers, like recordkeepers, from using participants' personal data to cross sell their own non-plan products.

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Participant Data Claims

- Since 2017, claimants have filed a waive of lawsuits against plan fiduciaries based on allegedly excessive investment management and administrative fees.

- In six 403(b) plan excessive fee cases, the plaintiffs sought amend their complaints to add participant data claims
  - Four cases settled before the claims were resolved;
  - One case is pending; and
  - In one case, the district court denied leave to amend, and the Seventh Circuit affirmed.

- In 2020, two 401(k) excessive fee cases were filed that included claims based on alleged misuse of participant data.

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Participant Data Claims

In re TIAA-CREF Indiv. & Inst. Services, LLC. (SEC 2019)

- In 2017, a non-ERISA whistleblower complaint was filed based on concerns about a third-party administrators' use of participant data.
- The whistleblower alleged that TIAA-CREF — a recordkeeper used by many 403(b) plans — used participants' data to push participants into their own, more expensive non-plan products.
- Participants cited articles about this whistleblower complaint and the allegations regarding cross-selling abuses to support their participant data allegations.

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Participant Data Claims

Divane v. Northwestern University (7th Cir. 2020)

- Participants sought to amend their complaint to add participant data claims.

- The district court denied leave to amend, noting:
  - Participants failed to "cite a single case in which a court has held that releasing confidential information or allowing someone to use confidential information constitutes a breach of fiduciary duty …or that such information is a plan asset in a prohibited transaction."
  - The district court found that plan fiduciaries did not breach their fiduciary duties by allowing access to participants' confidential information–required to perform necessary recordkeeping functions.

- The Seventh Circuit affirmed the district court's decision.

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Participant Data Claims

Berkelhammer v. ADP TotalSource Group (D. N.J. 2020)

- In 2020, participants filed a class action against ADP (the plan's sponsor) and NFR Retirement, Inc. (the investment consultant), which included participant data claims.

- ADP and NFR challenged the participants' standing and argued failure to state a claim on the basis that:
  - The only alleged injury is marketing communications,
  - There aren't any allegations that participants took any action because of marketing communications or were in fact solicited, and
  - Any incidental benefit to necessary recordkeeping transaction is not a prohibited transaction.

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Participant Data Claims

Harmon v. Shell Oil Co. (S.D. Tex. 2020)

- In 2020, participants filed a class action including participant data claims against Shell Oil and Fidelity (plan recordkeeper).

- In its motion to dismiss, Fidelity argues
  - Participants lack standing because no alleged harm,
  - Practical implications of finding participant data is a plan asset protected by ERISA are untenable, and
  - Weight of legal precedent supports finding against participants.

- Participants challenge Fidelity's position as inconsistent with prior non-ERISA litigation and internal memos treating customer information as proprietary information.

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Participant Data in Settlements

- Four recent settlement agreements in 403(b) excessive fee cases included participant data cross-selling restrictions in response to these emerging claims.

- These settlement provisions prohibit plan recordkeepers from:
  - "Us[ing] information received as a result of providing services to the Plans and/or the Plans' participants to **solicit the Plans' current participants** for the purpose of **cross-selling non-Plan products and services**, including, but not limited to, Individual Retirement Accounts ('IRAs'), non-Plan managed account services, life or disability insurance, investment products, and wealth management services, **unless in response to a request by a Plan participant."**

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Fraud and Cybersecurity

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Fraud and Cybersecurity

- According to the Federal Trade Commission, there were more than 172,000 fraud reports filed in the first six months of the pandemic.
- Remote work increases potential for attacks aimed at plan sponsors, service providers, and participants.
- Claims related to fraud and cybersecurity issues have found their way into ERISA fiduciary breach litigation.

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Fraud and Cybersecurity

Leventhal v. The MandMarblestone Group (E.D. PA 2020)

- Participant, 401(k) plan, and sponsor filed suit against third-party administrator, MandMarblestone Group ("MMG"), and asset custodian, Nationwide, after cyber criminals stole money from the participant's plan account.
- Participant, Jess Leventhal, was a principal of the plan sponsor (a law firm), and a trustee and fiduciary of the plan.
- Participant made a legitimate withdrawal from account, then "unknown criminals" obtained copy of the withdrawal form and "posed electronically" as participant.

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Fraud and Cybersecurity

Leventhal v. The MandMarblestone Group (E.D. PA 2020)

- Cyber criminals sent further withdrawal request forms to MMG that appeared to have originated from the participant's office email account.
- Multiple fraudulent withdrawal requests were made in high frequency.
- Requests sought distributions to a bank account that was not previously linked to the participant.
- Participant's 401(k) account was reduced from $400,000 to $0.

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Fraud and Cybersecurity

Leventhal v. The MandMarblestone Group (E.D. PA 2020)

- Plaintiffs claimed MMG documents showed that it was aware of the "peculiar nature" and frequency of the fraudulent withdrawals.
- Alleged Nationwide improperly distributed the funds to a bank account that was not previously linked to the participant and failed to authenticate withdrawal and signature forms.
- Further alleged that neither Defendant implemented "commonly employed procedures and safeguards" to notify the plaintiffs of these strange requests and/or verify their authenticity.

Fraud and Cybersecurity

Leventhal v. The MandMarblestone Group (E.D. PA 2020)

- Plaintiffs brought an ERISA breach of fiduciary duty claim and two state law claims for breach of contract and negligence.
- Court found state law claims were preempted by ERISA.
- Defendants moved to dismiss federal ERISA claim on basis that:
  - MMG and Nationwide were not fiduciaries because they did not have "discretionary authority or control" over plan assets,
  - There was no duty under ERISA for MMG to secure the plaintiffs' IT systems or for Nationwide to prevent forgeries, and
  - Nationwide's services agreement disclaimed liability.

Fraud and Cybersecurity

Leventhal v. The MandMarblestone Group (E.D. PA 2020)

- In its decision, the court noted that an entity may be considered an ERISA fiduciary if they are (1) a named fiduciary under the plan; or (2) if the entity "functions" as a fiduciary.

- Court concluded that MMG was a fiduciary because it was named as a fiduciary in the Nationwide Agreement.

- Nationwide was also a fiduciary because it had "actual control" over the plan's assets (i.e. the money) and because it was in position to distribute and dispose of those funds.

Fraud and Cybersecurity

Leventhal v. The MandMarblestone Group (E.D. PA 2020)

- Court found that the plaintiffs sufficiently alleged fiduciary breach claim based on allegations that MMG and Nationwide failed to act, despite suspicious actively.
  - "Peculiar nature" and high frequency of withdrawal requests,
  - That funds were distributed to a new bank account, and
  - Failing to alert the plaintiffs or verify the requests.

- Court rejected Nationwide's argument that services agreement disclaimed liability because ERISA prohibits disclaiming fiduciary liability under ERISA § 410(a).

Fraud and Cybersecurity

Leventhal v. The MandMarblestone Group (E.D. PA 2020)

- With its answer, MMG asserted counterclaims against the plaintiffs for contribution and contractual indemnification.
- Claimed plaintiffs' carelessness with respect to employees, computer/IT systems, and policies contributed to theft.
- Third Circuit has not decided whether contribution or indemnity claims exist under ERISA, and other circuits split;
  - Allowed in 2nd and 7th, but preempted in 8th and 9th Circuits.
- Court "persuaded by district court authority" that contribution and indemnity claims were available, and let claims proceed.

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Fraud and Cybersecurity

Leventhal v. The MandMarblestone Group (E.D. PA 2020)

- Nationwide answered complaint, but asserted a third-party complaint against "Texas Defendants" alleging that they were the cyber criminals that conspired to defraud the plan.
- Court struck ERISA contribution/indemnity claim against Texas Defendants because no allegations that they were plan fiduciaries and/or parties in interest.
- Struck remaining conspiracy and aiding and abetting claims against Texas Defendants because it would complicate case.
- Case settled after some discovery.

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Fraud and Cybersecurity

Berman v. Estee Lauder Inc. (N.D. Cal. 2019)

- Claims based on theft of $99,000 from the participant's account in three separate unauthorized distributions.

- Plaintiff claimed that, by the time she received the first mailed distribution notice, all three fraudulent distributions had been completed.

Fraud and Cybersecurity

Berman v. Estee Lauder Inc. (N.D. Cal. 2019)

- Estee Lauder and plan committee sued for alleged breach of fiduciary duty as ERISA fiduciaries.
- Alight Solutions sued as an alleged fiduciary because it provided administration, recordkeeping, and information management services to the Plan.
- State Street, the custodian of the plan's assets, sued as an alleged fiduciary because it provided investment management services to the plan.

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Fraud and Cybersecurity

Berman v. Estee Lauder Inc. (N.D. Cal. 2019)

- Plaintiff alleged that the plan imprudently and disloyally allowed her 401(k) account to be fraudulently distributed in the three transactions.
- Document penalties claim for alleged failure to provide plan documents.
- Case settled before any challenge to the plaintiffs' claims.

Fraud and Cybersecurity

Bartnett v. Abbott Laboratories (N.D. Ill. 2020)

- Participant in Abbott's 401(k) plan brought breach of fiduciary duty action against plan sponsor (Abbott Labs), the plan's administrator and named fiduciary (Marlon Sullivan), and the plan's recordkeeper (Alight Solutions).

- Participant alleged that an impersonator:
  - Accessed her plan account online through Alight website;
  - Added a new bank account on the Alight website;
  - Requested a $245,000 distribution from the 401(k) plan's recordkeeper, Alight to be deposited into the new account; and
  - Called Alight several times to ask questions about obtaining the distribution.

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Fraud and Cybersecurity

Bartnett v. Abbott Laboratories (N.D. Ill. 2020)

- Alleged missteps by defendants included:
  - Failure to recognize that the phone number used by the impersonator was not associated with the account;
  - Failing to identify and halt suspicious distribution requests (i.e. addition of new bank account followed by a substantial distribution);
  - Customer service representative's reading of Participant's mailing address to the impersonator in two separate phone calls; and
  - Failure to use Participant's preferred method of communication (email) by sending notices via regular mail re newly added direct deposit bank account and ultimately re the distribution.

- Breach of fiduciary duty under ERISA section 502(a)(2); violation of Consumer Fraud and Deceptive Practices Act.

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Fraud and Cybersecurity

Bartnett v. Abbott Laboratories (N.D. Ill. 2020)

- In ruling on motions to dismiss, district court dismissed claims against Abbott Labs and Sullivan, but not against Alight:
  - Complaint fails to allege any fiduciary acts taken by Abbott Labs, no less link them to the alleged theft;
  - While the complaint alleges that the call center and website were used to perpetuate the theft, it also indicates that both are operated by Alight (not Abbott Labs or Sullivan);
  - The duty of prudence did not extent to "safeguarding of data and prevention of scams";
  - Plaintiff did not allege that Abbott Labs and Sullivan should have been aware of the risk with Alight; and
  - Alight is a fiduciary due to discretionary control over plan assets.

Fraud and Cybersecurity

Bartnett v. Abbott Laboratories (N.D. Ill. 2020)

- Participant amended the complaint to include claims against Abbott Labs and Sullivan alleging breach of the duty of loyalty or the duty to monitor Alight.
  - Participant alleges that Abbott Labs and Sullivan should not have rehired Alight in 2015 or kept Alight due to numerous red flags.

- On February 8, 2021, District Court dismissed claims against Abbott Labs and Sullivan for a second time:
  - Most of the red flags that participant raises regarding Alight occurred after rehired and/or after participant's plan assets were stolen; and
  - Abbott Labs and Sullivan did not have sufficient information about issues with Alight as to the Abbott plan before alleged theft occurred.

Fraud and Cybersecurity

Bartnett v. Abbott Laboratories (N.D. Ill. 2020)

- Heading to settlement conference in early April 2021.
- Plaintiff given opportunity to seek leave to amend 30 days after defendants substantially complete document production if the case does not settle at the settlement conference.

Lessons Learned & Fiduciary Best Practices

Lessons Learned & Fiduciary Best Practices

Participant Data

- Review recordkeeping and other service provider agreements to determine whether plan prohibits using participant data for cross-selling non-plan products.
- Inquire whether participant data is being used to cross-sell non-plan products.
- Consider whether to include restrictions on use of participant data in service agreements with potential service providers, like recordkeepers.

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Lessons Learned & Fiduciary Best Practices

Fraud and Cybersecurity

- Verify service providers' cybersecurity protocols and obligations under operative agreements.
- Monitor service providers to make sure they are fulfilling their cybersecurity obligations.
- Review fiduciary liability coverage regarding losses due to cyber crimes, including fraud and theft.

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Lessons Learned & Fiduciary Best Practices

Fraud and Cybersecurity

- Educate participants on risks and best practices for accessing their plan information online.
- Review media and other news about plan security breaches.

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