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Client Alert

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401(k) Class-Action Litigation Update

By Richard J. Pearl

Many ERISA 401(k) plan trustees act as intermediaries when participants request a disbursement. If plan assets are invested in funds, some fund shares will be exchanged for cash, and the cash will then "float" as it makes its way from fund to participant. During that process, the float may sit temporarily in a non-plan, non-participant account, and it might earn interest.

Over the past several years, plaintiffs have alleged that the float constitutes a plan asset, and trustees who earned interest on the float breached their fiduciary duties by using the float to benefit themselves and not the plan. In *In re: Fidelity ERISA Float Litigation*, No. 15-1445 (1st Cir., July 13, 2016), the plaintiffs alleged that Fidelity breached its fiduciary duties because it used float to earn interest for itself, and not to benefit the plan. The money floated at two points in time: when Fidelity received the participants' cash and placed it in a temporary account, and, for those participants who requested paper checks and not electronic disbursements, when cash sat in a disbursement account until the participant cashed a paper check.

The district court dismissed the complaint on the defendants' motion to dismiss. The First Circuit, in a decision former Supreme Court Justice Souter wrote as he sat by designation, upheld the dismissal.

Plaintiffs Received Everything They Were Entitled To Receive

In the opinion's opening paragraphs, and again later in the opinion, the Court stressed that this case is not about direct injury to any plan participants. The participants admitted that they received penny-for-penny the exact value of funds allocated to their 401(k) accounts. The plan documents also did not entitle participants to interest earned on any float.

Float is not a Plan Asset

After explaining that individual participants did not lose a penny from the float, the Court disposed of the plaintiffs' argument that the float was a plan asset. ERISA doesn't define "plan asset" comprehensively. Instead, plan assets are identified according to "ordinary notions of property rights" under non-ERISA law. According to the plan documents and the actual manner in which funds were cashed out and distributed to participants, the funds were plan assets, but once cashed out, the payout never went and was never intended to go to the plan. When the plan instructed Fidelity to redeem shares, the plan was essentially asking Fidelity to pay the participant directly. The money as it moved through Fidelity to the participant did not become a plan asset just because it was in a fiduciary's hands; it was not a plan asset because it didn't belong to the plan. The plan documents themselves also prevented the trust from holding uninvested cash as plan assets, further supporting the Court's conclusion that the cash did not belong to the plan.

The plan documents also expressly required Fidelity to distribute withdrawals directly to participants, not to the plan. The plan did not bear the risk if the cash were lost after redemption but before the participant received it.

Did Fidelity Need Permission to Use Float?

The opinion mentioned, but did not decide, an argument the DOL made in an amicus brief. The DOL argued that even if the float was not a plan asset, ERISA's fiduciary duties required Fidelity to get the plans' permission to use the float as it did. By using assets to earn interest for itself, the DOL argued, Fidelity engaged in a prohibited transaction and acted disloyally.

The complaint, however, did not allege this theory of liability, and the plaintiffs waived it by not making it themselves. The Court did, however, note that it would consider the DOL's argument "in another case."

The Decision's Impact

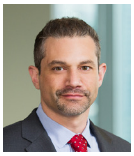
The Court's conclusion that float isn't a plan asset relied on the plan documents' express language and the fact that participants received the exact value of their fund allocation when the participants cashed out. Whether or not an asset is property of the plan, a participant, or someone else may depend on the language in the plan, how the assets actually were handled, and whether the participants received less than they were entitled to receive.

ERISA plan fiduciaries may want to review whether their plan involves periods of floating assets, whether agreements with service providers address how the float is to be handled, whether plan documents or information provided to participants address the float, and whether the float is being handled appropriately.

If you have any questions or would like assistance with any of the matters discussed in this alert, contact any member of our Employee Benefits and Executive Compensation Practice Group.

Employee Benefits and Executive Compensation Team

Primary Contact



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