Retirement Plan Fiduciaries Must Adjust to New Era of ERISA Litigation: How a Recent SCOTUS Ruling and $39M Jury Award Changed the Game

Insights
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A Supreme Court decision in April made it easier for plaintiffs to keep ERISA prohibited transaction claims in play longer, and just days later a rare ERISA trial resulted in a huge win for a class of 401(k) plan participants. What do retirement plan sponsors and fiduciaries need to know about this new era of ERISA litigation? We'll break it all down and give you some best practices to stay ahead of a potential new wave of litigation risks.

Snapshot of ERISA Fiduciary Rules

- **Fiduciary Status.** Generally, a person is a fiduciary of an ERISA-governed plan if they (1) exercise discretionary authority or control over plan management or plan assets; (2) have discretionary authority or responsibility for the plan's administration; or (3) give paid investment advice to a plan (or have any authority or responsibility to do so).
- **Fiduciary Duties.** Plan fiduciaries must follow certain principles of conduct when running the plan, including by acting prudently and solely in the interest of participants and beneficiaries and for the exclusive purpose of providing benefits and paying plan expenses – known as the **duties of loyalty and prudence** under ERISA §404(a).

- **Prohibited Transactions**. ERISA §406 prohibits plan fiduciaries from causing the plan to engage in certain types of transactions with any "party in interest" (such as a service provider for the plan, an employer that has employees covered by the plan, or another plan fiduciary), ***unless*** the transaction qualifies for an exemption under ERISA §408.

SCOTUS Just Made It Easier for Prohibited Transaction Claims to Survive Dismissal Stage

The Supreme Court's decision in *Cunningham v. Cornell University* may seem technical – as it focuses on how prohibited transaction claims are evaluated at the earliest stages of litigation – but the ruling creates serious concerns for fiduciaries and sponsors of ERISA retirement plans.

Snapshot of the Case

- **The Plans.** Cornell University sponsors two 403(b) defined contribution plans that are subject to ERISA. Each of the so-called "jumbo plans" holds over $1 billion in net assets.

- **The Claims.** Participants and beneficiaries of those plans sued the university and other plan fiduciaries, alleging in a 2017 complaint that the defendants **breached their duties of loyalty and prudence** by failing to control excessive recordkeeping fees and offering imprudent investment options, and that they **violated ERISA's prohibited transaction rules** by allowing the plans to be locked into those allegedly unreasonable arrangements.
- **The Lower Courts.** A federal court in New York largely **dismissed** (or granted summary judgment to defendants on) the claims, and the 2nd Circuit Court of Appeals **affirmed**.
- **The Key Issue.** In its 2023 decision, the 2nd Circuit held for the first time that, for a prohibited transaction claim to survive a defendant's motion to dismiss, "it is not enough to allege that a fiduciary caused the plan to compensate a service provider for its services; rather, the complaint must plausibly allege that the services were unnecessary or involved unreasonable compensation." In its reasoning, the appeals court said that the prohibitions under ERISA §406 must be read as incorporating the exemptions under ERISA §408 – otherwise, the court said, a vast array of routine transactions would be prohibited.
- **The Final Word**. The Supreme Court **reversed** that ruling in a unanimous April 17 decision written by Justice Sotomayor, holding that plaintiffs are **not** required to address potential exemptions under ERISA §408 in order for a prohibited transaction claim to make it past the motion-to-dismiss stage of litigation. Instead, **plaintiffs bringing such claims need only to plausibly allege the elements under ERISA §406**. The Court said that Section 406 "defines the offense" while "Congress wrote the §1108 exemptions in the orthodox format of an affirmative defense separate from the prohibitions." The case is now back at the district court level, where the plan fiduciaries will have the opportunity to raise a §408 exemption as an affirmative defense.

Key Implications for Plan Sponsors

- **Fewer ERISA lawsuits will be dismissed early.** The Court's decision lowers the bar for retirement plan participants to move past the motion to dismiss stage. That means more lawsuits may head into discovery – increasing legal costs and pressure to settle.
- **Fiduciary decision-making is more vulnerable to second-guessing.** Plan sponsors can't simply argue that their decisions were "within a reasonable range." If participants allege facts that suggest a lack of prudence – even if not definitive – the case may proceed.
- **More plan sponsors may face litigation.** This decision could lead to a wave of new ERISA lawsuits, especially targeting plans that offer retail share classes, have high administrative fees, or lack clear documentation of their fiduciary decision-making process.
- **Be ready to show *how* decisions were made, not just defend the outcomes.** The *Cornell* ruling reinforces a familiar truth for plan sponsors: *process matters*. Courts are more open to participant claims moving forward – and that means fiduciary decisions must be supported by clear, consistent, and well-documented reasoning. "It seemed reasonable at the time" won't cut it.

ERISA Jury Trial Sends Big Message: *Khan v. Bd. of Dirs. of Pentegra Defined Contribution Plan*

Just days after SCOTUS issued that decision, a federal jury considered whether 401(k) plan fiduciaries breached their duties under ERISA with respect to the plan's recordkeeping and administrative fees – and reached a landmark verdict in favor of the class of more than 25,000 participants.

Snapshot of the Case

- **The Plan**. Pentegra administers a defined contribution plan that is intended to be a multiple employer plan (MEP) under the Internal Revenue Code (26 U.S.C. §413(c)). MEPs allow unrelated employers to join together to offer a single retirement plan to their employees, and Pentegra's MEP is especially large – with more than $2 billion in assets and more than 25,000 participants. According to court filings, the plan sponsor is a board of directors consisting of executives from the various participating employers.
- **The Claims**: Participants in Pentegra's MEP filed suit in 2020 alleging that Pentegra and the plan's board of directors were plan fiduciaries and that they not only allowed excessive fees to be charged to the plan but used the plan to generate those fees to benefit itself. The participants claimed that the defendants therefore breached their fiduciary duties under ERISA and violated ERISA's prohibited transaction rules.
- **Jury Demand.** After years of complex pre-trial matters, a federal court in New York ruled in 2023 that the plaintiffs were entitled to a jury trial with respect to most of their claims – a rare occurrence in ERISA cases. Applying the two-part test laid out by the Supreme Court in 1989 for determining whether a lawsuit triggers the Seventh Amendment right to a jury trial, the court held that while breach of fiduciary *claims* are equitable in nature, the court would conduct a jury trial for claims seeking a legal *remedy*, which, according to the court, included the plaintiffs' requests to recover money damages out of the defendants' assets generally for all losses to the plan resulting from such breaches. In contrast, the court denied the plaintiffs' jury demand with respect to their claims for equitable relief, such as their request for removal of fiduciaries.

Jury Verdict: After a weeklong trial, a jury reached a verdict on April 23 in favor of the plan participants and found damages in the amount of nearly **$38.8 million**.

Key Implications for Plan Sponsors

- *Pentegra* could pave the way for more ERISA jury trials, especially within the 2nd Circuit, which has been more open than other courts to consider or grant jury trial requests in ERISA cases.
- More ERISA jury trials would mean increased litigation costs, which could indirectly harm participants if the plan or its sponsor has to bear the costs. Plan fiduciaries could also be exposed to greater personal liability if it will be up to a jury to determine if there's been any violation of the complex rules under ERISA.

- Plan fiduciaries may face increased scrutiny over selecting service providers that have (or appear to have) any affiliation with the plan sponsor, especially when a jumbo plan is involved.

Best Practices for Plan Sponsors

To stay ahead of litigation risks, plan sponsors should double down on fiduciary governance:

- **Document everything.** Keep clear, written records explaining why specific investments and service providers were selected — and why others were not.
- **Benchmark and review fees regularly.** Compare investment performance and administrative costs to industry standards and peer plans.
- **Use RFPs strategically.** Periodically run request-for-proposal (RFP) processes for recordkeepers and investment managers to demonstrate diligence.
- **Engage qualified experts.** Work with experienced consultants and advisors—and document your reliance on their input.
- **Train your fiduciary committee.** Make sure committee members understand their ERISA obligations and maintain minutes that reflect active, informed oversight.

Conclusion

We will continue to monitor developments related to ERISA litigation and all aspects of employee benefits law, so make sure you subscribe to Fisher Phillips' Insight System to get the most up-to-date information. If you have questions, contact your Fisher Phillips attorney, the author of this Insight, or any attorney on our Employee Benefits and Tax Practice Group.

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