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Third Circuit Holds That 401(k) Plan Participants Have Standing Under ERISA Section 502(a)(2)

On August 19, 2005, the Third Circuit issued its decision in *In re Schering-Plough Corp. ERISA Litigation,* 2005 WL 1993990 (3d Cir. Aug. 19, 2005). Reversing the district court, the Third Circuit ruled that 401(k) plan participants had standing to assert claims under ERISA § 502(a)(2), 29 U.S.C. § 1132(a)(2), for claims of breach of fiduciary duty relating to losses resulting from their investment in employer stock, even though not all participants experienced such losses.

Background

The underlying complaint alleged that the former CEO of Schering-Plough, the plan's fiduciaries, their counsel, and the trustee of the plan breached their fiduciary duties of prudence, care and loyalty in permitting the plan to offer as one of the plan's investment options a company stock fund invested in company stock; failing to disclose material adverse information relating to the alleged artificially inflated stock price; and failing to avoid conflicts of interest that inhibited defendants from properly performing as fiduciaries. The district court granted defendants' motion to dismiss on the grounds that plaintiffs were not seeking plan-wide relief but rather individualized relief, and, therefore, did not have standing to bring their claims under ERISA § 502(a)(2).

The Third Circuit's Decision

In holding that the complaint sought relief for the plan, and thus asserted viable claims under ERISA § 502(a)(2), the Third Circuit took note that ERISA § 409, 29 U.S.C. § 1109 — the provision providing for remedies under ERISA § 502(a)(2) — allows the plan to recover "any losses" from a breach of fiduciary duty. The Court concluded that this provision was broad enough to encompass claims seeking recovery of losses to some, but not all, participants of an individual account plan, particularly where, as here, those losses were experienced through investment in a fund that purchased stock on participants' behalf and that would be the initial source of any recovery prior to redistribution of the recovery to individual accounts.

The Third Circuit also rejected several arguments that had been embraced by the district court. First, the Court concluded that although *Massachusetts Mutual Life Ins. Co. v. Russell*, 473 U.S. 134 (1985), stated that any relief under ERISA § 502(a)(2) must inure "to the plan as a whole," it did so under circumstances that were not relevant here.

Second, relying on *In re Honeywell Int'l ERISA Litigation,* 2004 WL 3245931 (D.N.J. June 14, 2004), the Court concluded that just because plaintiffs may have to show individual reliance on the defendants' alleged misrepresentations to prevail on some claims does not mean they do not seek recovery for plan losses.

Third, the Court rejected the argument that the claims should be dismissed for failure to withstand a presumption favoring stock investments that the Third Circuit previously recognized in *Moench v. Robertson*, 62 F.3d 553 (3d Cir. 1995). In *Moench*, the Third Circuit held that "an ESOP fiduciary who invests the assets in employer stock is entitled to a presumption that it acted consistently with ERISA by virtue of that decision." The Court concluded that *Moench* was inapplicable because the plan in *Schering-Plough* did not involve an ESOP.

Finally, the Court found that the Fifth Circuit's decision in *Milofsky v. American Airlines, Inc.*, 404 F.3d 338 (5th Cir. 2005), *reh'g en banc granted and*

opinion vacated pending reh'g, No. 03-11087 (5th Cir. July 19, 2005) — in which a majority of the three-judge panel held that "plaintiffs lacked standing to bring a claim under ERISA § 502(a)(2) because this case in essence is about an alleged particularized harm targeting a specific subset of plan beneficiaries" — was factually distinguishable. The Third Circuit also agreed with the dissenting view of Chief Judge Carolyn King that plaintiffs need not seek relief for all participants of the plan in order to have standing under ERISA § 502(a)(2).

Implications For Employers & Fiduciaries

If the decision in *Schering-Plough* becomes the prevailing view regarding participant standing under ERISA § 502(a)(2) to sue for recoveries in 401(k) "stock drop" lawsuits, then it will effectively re-open a pathway to litigation that some believed might be closing in the wake of the Supreme Court's decision in *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204 (2002). In *Knudson*, the Supreme Court substantially curtailed recovery of monetary relief under ERISA § 502(a)(3), 29 U.S.C. § 1132(a)(3), which traditionally had been the avenue for individual participant claims for breach of fiduciary duty, by narrowly construing what constitutes "equitable relief." The plaintiffs' bar has responded to *Knudson* by relying increasingly on ERISA § 502(a)(2) as a vehicle for recovering monetary relief in 401(k) litigation and other suits seeking recovery of investment losses. A finding that standing was not available under ERISA § 502(a)(2) for participants of individual account plans, where not all participants experienced the same losses, would thus have constituted a devastating blow to the plaintiffs' bar.

Notwithstanding the *Schering-Plough* decision, the outcome of such claims in other Circuits remains uncertain. For instance, the Fifth Circuit has scheduled a rehearing *en banc* to determine the propriety of a district court's ruling denying standing to a sub-class of participants seeking to recover for investment losses in a defined contribution plan under ERISA § 502(a)(2). *See Milofsky v. American Airlines, Inc.*, 404 F.3d 338 (5th Cir. 2005), *reh'g en banc granted and opinion vacated pending reh'g*, No. 03-11087 (5th Cir. July 19, 2005). In a case handled by Proskauer Rose, the Fifth Circuit will also consider the propriety of certifying class claims under ERISA § 502(a)(2) where the relief sought is not for the benefit of all participants. *See In re Electronic Data Sys. ERISA Litig.*, 224 F.R.D. 613 (E.D. Tex. 2004), *appeal pending*, Case No. 04-41760 (5th Cir.); *see also Coan v. Kaufman*, 349 F. Supp. 2d 271, 274-277 (D. Conn. 2004), *appeal pending*, Case No. 05-1787 (2d Cir.).

The *Schering-Plough* decision may also have implications regarding the availability of a defense based on the *Moench* presumption in 401(k) cases. Although the Third Circuit's rationale is unclear, the decision in *dicta* purports to limit the availability of that defense to ESOP cases. If that limitation becomes the prevailing view, corporate and plan defendants will have lost an important vehicle for seeking the early dismissal of claims for fiduciary breach brought against 401(k) plan sponsors and fiduciaries.

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