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Tips For Settling An ERISA Class Action

By **Joseph Costello and Abbey Glenn** (April 23, 2020, 3:55 PM EDT)

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The recent stock market decline in the wake of the coronavirus crisis could lead to another wave of class actions under the Employee Retirement Income Security Act, challenging the prudence of investment options offered under 401(k) or other retirement plans. Most of these cases will be decided on motion or settled.

Settling an ERISA class action involves certain unique considerations that all parties should think through when finalizing the terms of a negotiated resolution.

Apart from the obvious points that need to be addressed in connection with any settlement — e.g., satisfying the requirements of Federal Rule of Civil Procedure 23, determining what role, if any, insurance will play in the funding of the settlement, providing for a plan of allocation to class members — ERISA class actions present additional issues that should not be overlooked.

What relief is contemplated by the settlement and how will it be implemented?

Most ERISA class action settlements provide for both monetary and nonmonetary relief. As to monetary relief, the settlement may be funded by the plan sponsor, by plan fiduciaries or service providers, by insurers, or by plan assets (or some mix of all of these). If the settlement contemplates the payment of plan assets (e.g, enhanced pension benefits), the plan administrator or fiduciary committee must approve the payment before agreeing to such relief (assuming the approving entity is not conflicted — see discussion regarding an independent fiduciary below).

Nonmonetary relief has evolved over time as plaintiffs seek more influence over post-litigation plan management, particularly where they allege that the plan fiduciaries employed a flawed or deficient plan oversight process. For instance, some settlements have required plan fiduciaries to conduct a request for proposals for plan record-keeping services and retain or continue to engage an independent investment adviser to provide ongoing investment monitoring services.[1]

Whatever the proposed affirmative relief, the parties should address how it will be implemented.

Does it require amending the plan and, if so, what are the steps needed to effectuate a plan amendment? How will ongoing plan oversight be affected? Will the plan record-keeper be involved in the allocation of settlement proceeds to plan participants and, if so, who will pay for that service? Will the proposed nonmonetary relief require external oversight by counsel and reporting to plaintiffs counsel?

Implementation of the relief negotiated by the parties could impose additional work on plan fiduciaries and their counsel, so that issue should be addressed in the settlement agreement itself to avoid later disputes that may undermine the settlement's finality.

Is approval by an independent fiduciary required?

The U.S. Department of Labor has concluded that a prohibited transaction occurs when a plan fiduciary causes a plan to release a claim against a person who is a party in interest at the time of the settlement.[2]

To overcome this hurdle and facilitate ERISA settlements in such circumstances, the Department of Labor issued Prohibited Transaction Exemption, or PTE, 2003-39, which covers the release of a plan's claims in exchange for consideration from a party in interest in partial or complete settlement of actual or threatened litigation.[3] The exemption requires a settlement to be approved and authorized by an independent fiduciary, which acts in the plan's interest and reviews the terms of the settlement to ensure it meets certain criteria.[4]

One settlement term that will be scrutinized by the independent fiduciary is the release. Once a case is dismissed, class members will be barred by res judicata from pursuing the same claims that were asserted or could have been asserted in the litigation against the same defendants. It is not unusual, however, for defendants to seek a release that also protects nonparties (e,g., fiduciaries, service providers, employees of the plan sponsor, insurers) and/or that encompasses claims that were not asserted in the litigation.

Whether the settlement is reasonable in the eyes of the independent fiduciary will depend, in part, on the scope of the release taking into account all relevant facts and circumstances under PTE 2003-39.

Recently, a class member in Cassell v. Vanderbilt University, in the U.S. District Court for the Middle District of Tennessee, objected to a proposed settlement of an ERISA class action involving fiduciary breach claims for offering allegedly expensive and underperforming investment options. The objector argued that the settlement's release was too broad because it included the plan's record-keepers, who were not sued and did not join or contribute to the settlement.[5]

The objector contended that the proposed settlement would release the record-keepers from any claims relating to their conduct in connection with the challenged investment options, foreclosing a potential source of recovery for plan participants. However, an independent fiduciary had already approved the release and issued a written determination that the objector's arguments did not alter its conclusion.

Ultimately, the objector withdrew his settlement challenge and the court approved the settlement. But the importance of the independent fiduciary's approval of the release cannot be overstated.

Does the settlement trigger other disclosures to participants or have an impact on other employee benefit plans?

In addition to any notice required by Federal Rule of Civil Procedure 23, ERISA may trigger an obligation to provide additional disclosures to plan participants.

For example, if the plan must be amended to comply with the settlement, the plan administrator may be responsible for publishing a summary plan description or a summary of material modifications that describes the relevant plan changes in terms that a reasonable person can understand. Some settlements may even address the content and timing of such disclosures.

The parties should also consider the impact of the settlement on other benefit plans that were not directly involved in the underlying litigation.

For example, some top-hat and collectively bargained plans contain what amount to #MeToo provisions linking the benefits thereunder to those provided by another plan. If the latter plan is amended due to the settlement, the terms or administration of the linked plans may need to change accordingly.

Also worth considering is whether any of the settlement's affirmative relief terms affect how the plan fiduciaries administer other benefit plans that were not at issue in the settled litigation.

For instance, if the settlement requires the fiduciaries to restrict how the record-keeper uses plan participant data in connection with one plan, the fiduciaries should consider whether to do the same with respect to all of the plans they oversee. Otherwise, there is risk that a participant in another plan discovers that the plan fiduciaries are safeguarding the information of participants in plans other than theirs and uses this against the fiduciaries.

Planning for Success

As Benjamin Franklin is credited for saying, "If you fail to plan, you plan to fail." Anticipating the above key issues will help insure a settlement that is free of unforeseen roadblocks and unintended consequences that could jeopardize judicial approval and impose additional effort and expense on both parties.

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[1] See, e.g., Tracey v. Mass. Institute of Tech., Case No. 1:16-cv-11620 (D. Mass. Oct. 28, 2019) docket entry 290-1; Cassell v. Vanderbilt Univ., Case No. 3:16-cv-2086 (M.D. Tenn. Apr. 23, 2019), docket entry 147-1; Short v. Brown Univ., Case No. 1:17-cv-00318 (D.R.I. Mar. 11, 2019), docket entry 45-2.

[2] In the DOL's view, such a settlement involves "an exchange of property (a chose in action) between such [plan] and parties in interest as described in ERISA § 406(a)(1)(A)." DOL Adv. Opinion 95-26A (Oct. 17, 1995).

[3] See PTE 2003-39, 68 Fed. Reg. 75,632 (2003).

[4] The settlement must be reasonable in light of the plan's likelihood of full recovery, the risks and costs

of litigation, and the value of claims foregone, and the terms and conditions of the transaction must be no less favorable to the plan than comparable arm's length terms and conditions that would have been agreed upon by unrelated parties under similar circumstances. See PTE 2003-39 §§ II(c), (d), 68 Fed. Reg. 75,639. In assessing reasonableness, the independent fiduciary must consider the entire settlement, including (1) the scope of the release of claims, (2) the value of any noncash assets to be received by the plan, and (3) the amount of any attorney's fee award or other sums to be paid from the recovery. See Adoption of Amendment to the Class Exemption for the Release of Claims and Extensions of Credit in Connection With Litigation (PTE 2003-39), 75 Fed. Reg. 33,830 (2010).

[5] Case No. 3:16-cv-2086 (M.D. Tenn. Oct. 2019), docket entries 158, 167-172.