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Publications

Groom Obtains Dismissal of Lawsuit Related to Use of Forfeitures

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PUBLISHED

09/16/2024

SOURCE

Groom Publication

SERVICES

Litigation

Employer & Sponsor Litigation

On September 5, 2024, a federal court for the Eastern District of Virginia dismissed claims that a 401(k) plan participant asserted against BAE Systems, Inc. regarding the use of forfeitures to reduce future employer contributions. The lawsuit is one of nearly twenty cases that have now been filed against large corporate plan sponsors related to the use of forfeitures. In the lawsuits, plaintiffs claim that using forfeitures to reduce future employer contributions is a breach of ERISA's fiduciary duties of loyalty and prudence, violates ERISA's anti-inurement provision, and constitutes a prohibited transaction under ERISA.

The Opinion

BAE Systems' 401(k) plan document expressly provided that forfeitures "shall" be used to 1) restore the accounts of participants who forfeited employer contributions by leaving the company before the contributions vested, but who rejoined the company within five years; and 2) reduce future employer contributions. The plaintiff argued that, despite the plan's mandatory language, forfeitures should have been used to pay administrative expenses or been credited to participants' individual accounts.

The Court squarely rejected plaintiff's argument, concluding that the plan language did not provide the fiduciary any choice with respect to how to use forfeitures. Specifically, the Court ruled "Plaintiff's position regarding forfeitures reduce to an argument that Defendant was required by ERISA to disregard the terms of the Plan and, contrary to the terms of the Plan, prioritize the use of forfeitures for, *inter alia*, the payment of administrative costs or a windfall to Plan participants, a proposition uniformly rejected by the courts."

The plaintiff also argued that another section of the plan document described that forfeitures "may" be used to pay administrative expenses and, as such, the fiduciary had discretion over how to use forfeitures. The Court also rejected this argument, explaining that the discretion in that provision was to be exercised in limited circumstances, such as where an employer suspends its contributions (e.g., as many companies did during the financial crisis).

As to plaintiff's claim that using forfeitures to offset employer contributions was a violation of ERISA's anti-inurement provision, the Court concluded the plaintiff failed to establish that plan assets were held for any reason other than to provide benefits to participants in the plan. Finally, with respect to the prohibited transaction claims, the Court held that the "settlor" act of establishing plan terms to direct how forfeitures are to be used cannot be a basis for a prohibited transaction claim.

Key Takeaways

The Court's ruling is a significant victory for defendants in the newest wave of ERISA litigation. The decision underscores that including plan terms that eliminate discretion by directing how forfeitures are to be used can mitigate litigation risk. The Court's recognition that the plan participants in these cases are essentially seeking a "windfall" is of equal importance and may be persuasive to courts considering similar claims.

Mike Prame, Nehama Hanoch, Rosemary Loehr, and Courtney Okwara represented BAE Systems, Inc. in the lawsuit.