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High Court’s Cornell Ruling Stands to Supercharge 401(k) Suits

Deep Dive

- **Benefit plans exposed to higher risk under pleading standard**
- **Court takes rare step, suggests methods for pumping brakes**

Workplace health or retirement plans that tap third-party service providers to deliver benefits are at high risk of having lawsuits against them fast-tracked to the costly discovery phase after a new US Supreme Court decision.

In a unanimous ruling April 17, the high court said that workers and retirees suing Cornell University for mismanaging a pair of retirement benefit plans only have to make a plausible allegation that the company engaged in a prohibited transaction under a federal benefits statute to survive a motion to dismiss.

Plaintiffs don’t have to prove that their employer was unqualified for one of hundreds of statutory or regulatory exemptions to the prohibited conduct, leaving the burden on the employer-sponsored plan to defend its transactions.

The employee-friendly ruling unlocks a new strategy for the plaintiffs' bar to expedite federal benefits law claims to discovery where the pressure on companies to settle ramps up and the penalties for noncompliance can skyrocket. It's a loss for employee benefit plans that raised alarms as appeals courts split on the prohibited transaction pleading issue.

"This means that plaintiffs can sue every defined contribution plan in the country and survive the motion to dismiss," said Kent Mason, outside counsel for the American Benefits Council and a partner at Davis & Harman LLP. It's a "sad day for ERISA plans," he added.

Associate Justice Sonia Sotomayor, writing for the majority, said the Employee Retirement Income Security Act separates prohibited transactions from their myriad exemptions, constituting affirmative defenses that are "the responsibility of the party raising them."

But at the same time, she conceded "serious concerns" that the court's ruling could lead to an "avalanche" of meritless litigation and took the rare step of outlining methods for district courts to apply the brakes.

Reform Calls

The ruling almost immediately prompted calls from the employer plan industry to pressure Congress, regulators, and the courts to reform and rethink ERISA pleading standards in a way that protects voluntary retirement plan sponsors held to strict fiduciary standards of conduct.

"They should push toward meaningful, prophylactic measures and legislative solutions or plan sponsors, service providers, and other regulated entities will be overwhelmed by litigation, and innovation will be stymied," said Will Delany, a principal and litigation co-chair at Groom Law Group Chartered.

Sotomayor's opinion suggested that district courts reviewing ERISA cases should begin using the "not commonly used" Federal Rule of Civil Procedure 7(a)(7), which permits judges to order a reply to the defense's answer. In such cases where prohibited transactions have been alleged, district courts could use the rule to determine whether a relevant exemption applied before reaching discovery.

"District courts should strongly consider utilizing this option—and employing the other safeguards that the Court describes—to achieve 'the prompt disposition of insubstantial claims,'" Associate Justice Samuel Alito wrote in a concurring opinion joined by Associate Justices Clarence Thomas and Brett Kavanaugh.

The Supreme Court case arose out of a US Court of Appeals for the Second Circuit decision that tried to balance splits between the Third, Seventh, Ninth, and Tenth circuits. The Second Circuit panel said it sought to stave off an "absurd" result it feared would trigger a wave of litigation against benefit plans.

That caught the attention of President Donald Trump's choice to lead the nation's top employee benefits regulator, insurance executive Daniel Aronowitz. He filed an amicus brief in the Supreme Court case, alleging that a lower pleading standard such as the one the high court reached would allow plans to be "sued at any time—essentially forced into a litigation audit by private lawyers."

But it seems unlikely that the court's guidance will be enough, said Carol Buckmann, a founder and partner at Cohen & Buckmann PC.

"Different judges are just that—different—and we're not going to get consistent controls on meritless litigation with these recommendations," she said.

Lawyers representing workers and retirees expressed less concern about the consequences of the high court's decision.

Plaintiffs' firms are business-oriented and "don't tend to chase cases unless there's money to be recovered," said Greg Porter, a Bailey & Glasser lawyer who represents plan participants in ERISA litigation. By that logic, it doesn't make sense for an attorney to tackle a case where a get-out-of-jail exemption is readily available, he said.

"There's going to be more litigation here, but it's not going to be a sea change," he said. "Cases are going to get a little farther along before the parties get together."

ERISA Law

Enacted in 1974 to defend against companies and unions tapping into pension funds as if they were operating reserves, ERISA treats virtually any transaction as a potential conflict of interest, and outright bans routine service-provider contracts such as recordkeeping.

A separate section later in the statute lays out 21 statutory exemptions for transactions that are "reasonable" or "necessary," and empowers the US Labor Department to issue more.

That separation—a few paragraphs of text between sections 406 and 408 in the law—means Congress intended the exemptions to be treated as affirmative defenses, shifting the responsibility to prove compliance from the plaintiffs to the defendants, the Supreme Court ruled.

Fifty years later, and the employee benefit plan landscape has changed.

"Every plan in the country needs outside service providers," said Buckmann. "ERISA and the tax code are so complex today that it's foolhardy to do this yourself. That just wasn't the case when ERISA was enacted."

Yet, the plaintiffs' bar developed a successful business at suing "unwary" benefit plans because some don't have in place a compliance paradigm rooted in clear, agreed-upon fiduciary decisionmaking, despite a general uptick in the number of ERISA claims filed, said Anne Tyler Hall, managing partner at Hall Benefits Law LLC.

"The plaintiffs bar is well-adept at searching for low-hanging fruit, and there's plenty of it," Hall said. "They're just doing their job, and they've found plenty of fertile territory."

The case is Cunningham v. Cornell Univ., 2025 BL 130356, U.S., 23-1007, 4/17/25.

To contact the reporter on this story: Austin R. Ramsey in Washington at aramsey@bloombergindustry.com

To contact the editors responsible for this story: Rebekah Mintzer at rmintzer@bloombergindustry.com; Jay-Anne B. Casuga at jcasuga@bloomberglaw.com