Arbitration of ERISA Retirement Plan Disputes

A Practical Guidance® Practice Note by
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This practice note discusses the general enforceability of arbitration clauses in certain disputes, including class actions, with a particular focus upon the enforceability of arbitration clauses involving legal claims made under the Employee Retirement Income Security Act (ERISA). This practice note also specifically analyzes the advantages and disadvantages of arbitration provisions for retirement plan sponsors.

The practice note is organized as follows:

- Arbitration Generally
- Arbitration of Class Actions Claims
- Arbitration of ERISA Claim Review Procedures
- Arbitration of Statutory ERISA Claims
- Arbitration in Employment Agreements Versus Plan Documents
- Advantages and Disadvantages of Mandatory Individualized Arbitration
- Multiemployer Withdrawal Liability Arbitration

For additional materials on arbitration, see ARTICLE: ERISA and Other Federal Employment Statutes: When Is Commercial Arbitration an "Adequate Substitute" for the Courts?, 68 Tex. L. Rev. 509; COMMENT: ERISA AND ARBITRATION: HOW SAFE IS YOUR 401(K)?, 64 DePaul L. Rev. 773; and Enforceability of pre-dispute agreements to arbitrate claims arising under Employee Retirement Income Security Act of 1974 (ERISA) (29 U.S.C. § 1001 et seq.), 116 A.L.R. Fed. 525. For additional Practical Guidance regarding ERISA litigation, see Standard of Review and Deference in ERISA Litigation and Statute of Limitations for ERISA Claims.

For more information on the different types of alternative dispute resolution (ADR) processes and procedures available to attorneys to resolve a legal dispute, see ADR Processes and Procedures (U.S.).

Arbitration Generally

Congress enacted the Federal Arbitration Act (FAA) in 1925 to reverse "longstanding judicial hostility to arbitration agreements." Green Tree Fin. Corp. Alabama v. Randolph, 531 U.S. 79, 80 (2000). The purpose of the FAA was to encourage arbitration of disputes because of the benefit of quicker, more informal, and often cheaper resolutions as compared to traditional litigation. Epic Sys. Corp. v. Lewis, 138 S. Ct. 1612 (2018). Congress passed the FAA to realize these objectives and make arbitration agreements valid, irrevocable, and enforceable. Id.

Section 2 is the core provision of the FAA. It states that "[a]written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of

such contract or transaction . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." Courts will consistently enforce Section 2 because of the "liberal federal policy" favoring mandatory arbitration. AT&T Mobility LLC v. Concepcion, 563 U.S. 333, 339 (2011) citing 9 U.S.C. § 2.

Litigation typically concerns the lawfulness of attempts to compel arbitration. To compel arbitration, a party need only show: (1) an agreement to arbitrate, (2) a dispute within the scope of the arbitration agreement, and (3) a refusal by the opposing party to proceed to arbitration. Unless any of the exceptions discussed below apply or a party has otherwise waived the right to arbitrate, courts generally rigorously enforce agreements to arbitrate to support the validity of bargained-for contracts and for policy reasons favoring economical and efficient resolutions of disputes.

Exceptions to Judicial Enforcement of Arbitration Agreements

The Supreme Court has repeatedly instructed that the FAA requires to courts to "rigorously enforce' arbitration agreements according to their terms," including agreements to arbitrate claims arising under federal statutes. Am. Express Co. v. Italian Colors Rest. 133 S. Ct. 2304, 2309, 186 L.Ed.2d 417 (2013) (quoting Dean Witter Reynolds Inc. v. Byrd, 470 U.S. 213, 221, 105 S. Ct. 1238, 84 L.Ed.2d 158 (1985)). There are, however, three separate exceptions courts could apply to find an agreement to arbitrate under the FAA unenforceable. The first exception is that the FAA's mandate is overridden where there exists a "contrary congressional command." CompuCredit Corp. v. Greenwood, 565 U.S. 95, 98 (2012). The second exception being that a mandatory arbitration agreement can be unenforceable if it is encompassed in Section 2's "savings clause." The savings clause states that a court can decline to enforce an arbitration agreement based on "generally applicable" contract defenses that would be applicable to any commercial contract. Concepcion, 563 U.S. at 35. The Supreme Court has made clear, however, that if a defense normally thought to be generally applicable to contracts (such as fraud, duress, unconscionability, or illegality) is applied in a way that targets or uniquely disfavors arbitration, the defense will not render the arbitration agreement unenforceable. The third exception is the "effective vindication" exception, which originated as dictum in Mitsubishi Corp. v. Soler Chrysler Plymouth, Inc., 473 U.S. 614 (1985). That exception comes from a desire to prevent "prospective waiver of a party's right to pursue statutory remedies." Mitsubishi Corp., 473 U.S. at 637, n.19. *See also* Italian Colors, 570 U.S. at 236 (noting that "an arbitration agreement forbidding the assertion of certain statutory rights" cannot be enforced).

In the context of agreements to arbitrate ERISA claims the first two exceptions are generally inapplicable. Every circuit court of appeals to consider the question has held that ERISA contains no "congressional command" against arbitration. See Dorman v. Charles Schwab Corp., 780 Fed. Appx. 510, 513-514 (9th Cir. 2019). Further, because litigation of ERISA claims typically does not involve "generally applicable" common law contract defenses the second exception is rarely invoked.

The "effective vindication" exception, however, may be applicable to ERISA claims, particularly with respect to breach of fiduciary duty claims brought pursuant to ERISA Section 502(a)(2). In Cooper v. Ruane Cunniff & Goldfarb Inc., 990 F.3d 173 (2d Cir. 2021), for example, a divided Second Circuit Court of Appeals determined that a class arbitration waiver "would not necessarily eliminate" the right to bring a claim under ERISA Section 502(a)(2) because of the "effective vindication" exception set forth by the Supreme Court in *Italian Colors*. See Cooper, 990 F.3d 184-185. The Second Circuit declined to effectively rule on the issue but reasoned that a participant's statutory right to bring a representative claim pursuant to ERISA Section 502(a)(2) and obligation to serve as a suitable representative of other stakeholders in such a claim, conflicted with the arbitration agreement in the matter. While the Second Circuit abdicated from ruling directly on the issue, later in 2021, the Seventh Circuit did not. The Court in Smith v. Bd. of Dirs. of Triad Mfg., Inc. 13 F. 4th 613,, 2021 U.S. App. LEXIS 27312 (7th Cir. 2021) applied the effective vindication exception to hold that an ERISA plan arbitration provision was unenforceable where it precluded the plaintiff from seeking plan-wide relief guaranteed by ERISA §§ 502(a)(2) and 409(a) (29 U.S.C. §§ 1132(a)(2) and 1109(a)). The arbitration language at issue in *Smith* purported to apply to all ERISA violations (and other claims) arising under the plan and expressly provided that all claims must be brought in the claimant's individual capacity and prohibited any form of relief or remedy having the purpose or effect of providing additional benefits or monetary or other relief to others. As discussed below, because of the major implications widespread adoption of the "effective vindication" exception would have for high-stakes breach of fiduciary class action litigation, the extension of the Seventh Circuit's *Smith* decision will likely be a hotly debated issue going forward.

Procedural Issues regarding Arbitration Clauses

As discussed above, the Federal Arbitration Act (FAA), which governs the enforceability of arbitration agreements, "evinces a national policy favoring arbitration," and requires federal courts "to place arbitration agreements on an equal footing with other contracts and enforce them according to their terms." A.D. v. Credit One Bank, N.A., 885 F.3d 1054 (7th Cir. 2018). The FAA provides that a party aggrieved by the alleged failure of another to arbitrate under a written agreement may petition a district court for an order compelling arbitration. To compel arbitration, a moving party must establish three items:

- An enforceable arbitration agreement
- A dispute within the scope of the arbitration agreement –and–
- The opposing party's refusal to arbitrate

Zurich Amer. Ins. Co v. Watts Industries, Inc., 466 F.3d 577, 580 (7th Cir. 2006). Once a party seeking arbitration has established these three elements, the burden shifts to the party opposing arbitration to demonstrate that the agreement is unenforceable or that the claims are not suitable for arbitration. Mecum v. Weilert Custom Houses, LLC, 239 F. Supp. 3d 1093, 1095 (N.D. Ill. 2017); Smith v. GreatBanc Trust Company, 2020 U.S. Dist. LEXIS 151992 (N.D. Ill. 2020).

The divided decision by the Court of Appeals for the Second Circuit in Cooper v. Ruane Cunniff & Goldfarb Inc., 990 F.3d 173 (2d Cir. 2021), indicates that it may be a close question as to whether a particular dispute is within the scope of the arbitration agreement.

Attorney disqualification issues are better addressed by courts rather than arbitrators. Canfield v. SS&C Techs. Holdings, Inc., 2021 U.S. Dist. LEXIS 49800 (S.D. N.Y. 2021); Northwestern National Ins. Co. v. Insco Ltd., 2011 U.S. Dist. LEXIS 113626 (S.D.N.Y. 2011); Munich Reinsurance America, Inc. v. Ace Property & Casualty Ins. Co., 500 F. Supp. 2d. 272, 275 (S.D.N.Y. 2007); Troika Media Group, Inc. v. Stephenson, 2019 U.S. Dist. LEXIS 188277 (S.D.N.Y. 2019).

A circuit court exercises plenary review over a district court order compelling arbitration. Bouriez v. Carnegie Mellon University, 359 F.3d 292, 294 (3d Cir. 2004).

Considerations Affecting Arbitration Provisions

Generally applicable state law contract defenses such as fraud, duress, mistake, lack of consideration, or mutual obligation or unconscionability may invalidate an arbitration agreement. Cooper v. MRM Inv. Co., 367 F.3d 493, 498 (6th Cir. 2004). The FAA reflects the fundamental principle that arbitration is a matter of contract. Rent-A-Center, West, Inc. v. Jackson, 561 U.S. 63 (2010).

The fact that parties have agreed to arbitrate some disputes does not necessarily manifest an intent to arbitrate every dispute that might arise between the parties, because, under the FAA, parties are generally free to structure their arbitration agreements as they see fit. Volt Info Scis., Inc. v. Board of Trustees of the Leland Stanford Junior University, 489 U.S. 468 (1989).

Whether a dispute falls within the scope of an arbitration agreement depends upon the relationship between (1) the breadth of the arbitration clause and (2) the nature of the given claim. CardioNet, Inc. v. Cigna Health Corp., 751 F.3d 165 (3d Cir. 2014). While the Supreme Court stated in Moses H. Cone Memorial Hospital v. Mercury Construction Corp., 460 U.S. 1, 24-25 (1983) that a court must resolve "any doubts concerning the scope of arbitrable issues . . . in favor of arbitration," the Supreme Court has warned against overreading its precedent concerning the presumption of arbitrability. In Granite Rock Co. v. Int'l Brotherhood of Teamsters, 561 U.S. 287 (2010), the Supreme Court stated that the presumption in favor of arbitrability does not take courts outside the settled framework of using principles of contract interpretation to determine the scope of an arbitration clause. See also Sweet Dreams Unlimited, Inc., v. Dial-A-Mattress International, Ltd., 1 F.3d 639, 641 (7th Cir. 1993) ("While the FAA embodies a strong federal policy in favor of arbitration, . . . the duty to arbitrate remains one assumed by contract."). Thus, the presumption of arbitrability applies only where an arbitration agreement is ambiguous about whether it covers the dispute at hand. Otherwise, the plain language of the contract controls. See *CardioNet* and *Granite Rock*.

In determining whether a particular dispute falls within the scope of an arbitration clause, courts "focus on the factual underpinnings of the claim rather than the legal theory alleged in the complaint." Medtronic Ave. Inc. v. Advanced Cardiovascular Systems, Inc., 247 F.3d 4455 (3d Cir. 2001). As explained by the Tenth Circuit, the purpose of making a determination in this manner is to "prevent a creative and artful pleader from drafting around an otherwise applicable arbitration clause." Chelsea Family Pharmacy, PLLC v. Medco Health Solutions, Inc., 567 F.3d 1191, 1198 (10th Cir. 2009).

While there is a strong federal policy involving arbitration, that policy does not apply to a determination whether there is a valid agreement to arbitrate. O'Shaughnessy v. Young Living Essential Oils, LC, 2019 U.S. Dist. LEXIS 180503 (W.D. Tex. 2019).

When considering a motion to stay judicial proceedings and compel arbitration under the Federal Arbitration Act, a district court has four tasks:

- To determine whether the parties agreed to arbitrate
- To determine the scope of the arbitration agreement
- If federal statutory claims are asserted, it must determine whether Congress intended these claims to be arbitrable
- If some but not all of the claims are subject to arbitration, to determine whether the court should stay the remainder of the proceedings pending arbitration

Stout v. J.D. Byrider, 228 F.3d 709, 714 (6th Cir. 2000). The test for arbitrability is whether the parties consented to arbitrate the dispute in question. Granite Rock Co. v. Int'l Bhd. of Teamsters, 561 U.S. 287, 304, n.11 (2010). Because, under the FAA, contract law is left primarily to the states, the antecedent question of whether an enforceable contract or agreement to arbitrate exists, along with the interpretation of the contract or agreement, is generally a matter of state law. Hornsby v. Macon County Greyhound Park, Inc., 2012 U.S. Dist. LEXIS 81552 (M.D. Ala. 2012). See also Coleman v. Reliance Trust Co., 2019 U.S. Dist. LEXIS 223195 (E.D. Tex. 2019) (whether a particular dispute falls with the scope of an arbitration agreement is a question of state contract law, governed by federal arbitration law and policy) and Wisc. Local Govt. Property Insurance Fund v. Lexington Ins. Co., 840 F.3d 411, 414 (7th Cir. 2016) (whether the parties have agreed to arbitrate is a question normally answered by a court, with the issue governed by state law principles of contract formation).

In determining the scope of an arbitration agreement that falls under FAA, courts have held that all doubts regarding the scope of an arbitration agreement should be resolved in favor of arbitration. Coleman v. Reliance Trust Co., 2019 U.S. Dist. LEXIS 223195 (E.D. Tex. 2019). As the Court of Appeals for the Sixth Circuit stated in Nestle Waters No. American, Inc. v. Bowman, 505 F.3d 498, 504 (6th Cir. 2007), "Any doubts are to be resolved in favor of arbitration unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute."

In the vast majority of cases, the arbitrability of a dispute is a question for judicial determination. First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938, 944 (1995) and AT&T Techs, Inc. v Communications Workers of America, 475 U.S. 643, 649 (1986). However, while arbitrability issues are generally decided by courts, in Henry Schein, Inc. v. Archer and White Sales, Inc., 139 S. Ct. 524 (2019), the Supreme Court held that parties may agree to have an arbitrator decide not only the merits of a particular dispute but also gateway questions of arbitrability, such as whether the parties have agreed to arbitrate or whether their agreement covers a particular controversy.

On January 25, 2021, the Supreme Court dismissed as improvidently granted a writ of certiorari previously granted on a petition asking it to consider "whether a provision in an arbitration agreement that exempts certain claims from arbitration negates an otherwise clear and unmistakable delegation of questions of arbitrability to an arbitrator." Henry Schein, Inc. v. Archer & White Sales, Inc., 592 U.S. ___, 139 S. Ct. 524 (2021) ("Henry II").

In Hendricks v. UBS Financial Serv., Inc., 546 Fed. Appx. 514 (5th Cir. 2013), the Court of Appeals for the Fifth Circuit held that while the arbitration provision in the plan was enforceable, the scope of the provision, namely, whether class actions were prohibited or could be arbitrated, was a decision for the arbitrator.

Applicable Legal Standard in Judicial Review of Arbitration Provisions

Under Section 6 of the FAA, a request for relief under Section 4 is treated as a motion, but not further described. There are two different legal standards that a court may apply in reviewing a motion to compel arbitration. It is generally treated as a motion to dismiss for failure to state a claim upon which relief can be granted under Federal Rule of Civil Procedure (FRCP) 12(b)(6), while other cases indicate a district court should employ the standard used in resolving summary judgment motions pursuant to Fed. R. Civ. P. 56. See Guidotti v. Legal Helpers Debt Resolution, L.L.C., 716 F.3d 764, 771 (3d Cir. 2013) (discussing Third Circuit precedent) and Coleman v. Reliance Trust Co., 2019 U.S. Dist. LEXIS 223195 (E.D. Tex. 2019), discussing Fifth Circuit precedents.

Section 4 of the FAA provides that "if the making of the arbitration agreement or the failure, neglect, or refusal to perform the same [is] at issue, the court shall proceed summarily to the trial thereof. If no jury trial be demanded by the party alleged to be in default . . . the court shall hear and determine such issue." Dalon v. Ruleville Nursing and Rehabilitation Center, LLC, 161 F. Supp. 3d 406, 411 (N.D. Miss. 2016). A party seeking to avoid arbitration has the initial burden of production in order to create a fact issue on the validity of the arbitration clause. Gilliam v. Global Leak Detection U.S.A., Inc., 141 F. Supp. 2d. 734, 737 (S.D. Tex. 2001).

In Chester v. DirecTV LLC, 607 Fed. Appx. 362 (5th Cir. 2015), the Court of Appeals for the Fifth Circuit concluded that a plaintiff's affidavit stating that he did not sign the arbitration agreement was sufficient evidence to satisfy his threshold burden and put the making of an arbitration agreement in issue. Other courts have stated that a party contesting the making of an arbitration agreement must make at least some showing that under prevailing law he would be relieved of the contractual obligation to arbitrate if his or her allegations proved to be true, and also produce some evidence to substantiate his factual allegations. See *American Heritage Life Ins. Co. v. Orr*.

In Vaden v. Discover Bank, 556 U.S. 49 (2009), the Supreme Court held that federal jurisdiction in an action to compel arbitration under Section 4 of the FAA is determined by looking through the petition to the jurisdictional basis of the underlying substantive controversy. For example, if the underlying dispute between the parties falls within the court's jurisdiction by presenting a federal question then a court could rule on the petition to compel arbitration.

However, in Badgerow v. Walters, 142 S. Ct. 1310, 1321-22 (2022) in an 8-1 decision, the Supreme Court held that the approach in *Vaden* taken with respect to Section 4 of the FAA does not apply to orders to vacate an award of the FAA. As a result, in almost all instances, unless there is diversity jurisdiction, the review of the arbitrator's decision will take place in state court. In order for diversity jurisdiction to be available, complete diversity must exist, *i.e.*, a plaintiff must reside in a different state than any defendant.

It is also worth noting in this context that in Hall Street Associates v. Mattel, 552 U.S. 576 (2007), the Supreme Court held that Sections 10 and 11 of the FAA were the exclusive means of judicial review to vacate or modify an arbitration award. That decision though left unresolved whether other bases for review of arbitrators' awards, based upon common law and/or judicially created exceptions such as manifest errors of law or public policy challenges continued to be available. As the New Jersey District Court stated in Caputo v. Wells Fargo Advisors, LLC, No. 19-17204 (FLW), 2020 U.S. Dist. LEXIS 93856, at *7 (D.N.J. May 29, 2020): " [T]he circuit Courts of Appeal have ... disagreed on whether the public policy exception continues to serve as a cognizable basis for challenging an arbitrator's award." Even though different circuits maintain different standards for whether common law or judicially created exceptions are available to modify or vacate arbitration awards,the Supreme Court has twice denied certiorari on petitions to resolve this Circuit split.

Waiver of Arbitration Rights

Like all contract rights, the right to arbitrate a dispute is subject to a party waiving those rights through disregarding an agreement to arbitrate and litigating the matter in court. Nicholas v. KBR, Inc., 565 F.3d 904, 907 (5th Cir. 2009). A recent Supreme Court decision held that proving a party's waiver of arbitration rights can be shown without a special showing of prejudice and that the test for waiver of arbitration rights is no different than the test for waiver of any other litigation rights. ***See*** Morgan v. Sundance, Inc., 212 L. Ed. 2d 753, 142 S. Ct. 1708, 1714 (2022). In Sundance, the Supreme Court rejected a special showing of prejudice to apply and remanded the case bac to the Eighth Circuit so the Eighth Circuit could apply its basic test for waiver *e.g.* did a party knowingly relinquish the right to arbitrate by acting inconsistently with that right? *Id.* Therefore, practically this means that if a party wants to take advantage of any agreement to arbitrate it should do so at the earliest instant to avoid potential arguments of waiver.

Waiver of Jury Trial

Although the FAA permits parties to demand a jury trial to resolve factual issues surrounding the making of an arbitration agreement or the failure, neglect, or refusal to perform the agreement, a party to an arbitration agreement cannot obtain a jury trial merely by demanding one. American Heritage Life Ins. Co. v. Orr, 294 F.3d 702, 710 (5th Cir. 1992). A general jury demand in a complaint does not obviate the need specifically to request a jury trial under Section 4 of the FAA. King v. Capital One Bank (USA), 2012 U.S. Dist. LEXIS 137219 (W.D. Va. 2012). Where a jury trial has not been demanded, a district court may satisfy its duty under Section 4 of the FAA by holding an evidentiary hearing, but it does not necessarily need to do so. Chester v. DirecTV, L.L.C., 607 Fed. Appx. 362, 365 (5th Cir. 2015). Although the language in Section 4 of the FAA, "shall hear the parties," indicates that a live evidentiary hearing is requested, a "hearing on the papers may be all that is required." Marks 3-Zet-ErnstMarks GmBh & Co. v. Presstek, Inc., 455 F.3d 7, 14 (1st Cir. 2005). Even when the making of an arbitration agreement is at issue, a district court may determine the existence of an arbitration agreement based upon a paper record if either the evidentiary record reveals no genuine issue of material fact (see, e.g., Howard v. Ferrellgas Partners, LP, 748 F.3d 975 (10th Cir. 2014)) or the parties were afforded a sufficient opportunity to argue and develop the evidentiary record. U.S. Titan, Inc., v. Guangzhou Zhen Hua Shipping Co., 241 F.3d 135, 145 (2d Cir. 2001).

As a procedural matter, a court will first decide, based on the evidentiary record, whether the making of an arbitration agreement is an issue before the court. If it is not, the court can turn to the merits of the dispute. However, if the making of the arbitration agreement is in issue, the court must first decide whether an evidentiary hearing is necessary for a resolution on the merits. Reliance Trust Co., 2019 U.S. Dist. LEXIS 223195; Ruleville and Nursing Rehabilitation Center, LLC, 161 F. Supp. 3d 406.

Is Signature Required to Create a Valid Agreement?

Whether a signature is required to establish a valid arbitration agreement is a question of state law and generally a question of intent. Tricon Energy Ltd. v. Vinmar International, Ltd., 718 F.3d 448 (5th Cir. 2013). Thus, signatures are not required as long as the parties gave their consent to the terms of the agreement, and there is no evidence of an intent to require both signatures as a condition precedent to it becoming effective as a contract. Perez v. Lemarroy, 592 F. Supp. 2d. 924 (S.D. Tex. 2008). In the tax-qualified plan context, continuing in employment can establish consent. With respect to terminated vested participants who do not elect to receive a distribution from the plan, and thereby remain plan participants as defined under ERISA, it is an unresolved issue whether continued plan participation is sufficient to establish consent with respect to a plan amendment adopted after the participant terminated employment.

The FAA does not require that the agreement calling for arbitration be signed by both parties, but the party filing the motion to compel arbitration still has the burden of providing some other evidence to prove the party unconditionally and mutually assented to the terms of the contract. Rocha v. Macy's Retail Holdings, Inc., 2017 U.S. Dist. LEXIS 163918 (W.D. Tex. 2017).

In *Arthur Andersen, LLP v. Carlisle*, the Supreme Court recognized six circumstances that would allow a non-signatory to invoke an arbitration agreement: assumption, piercing the corporate veil, alter ego, incorporation by reference, third-party beneficiary theories, and estoppel. Arthur Andersen LLP v. Carlisle, 556 U.S. 624 (2009).

Note that, in Janvey v. Alguire, 847 F.3d 231, 242-43, cert. denied, 138 S. Ct. 329 (2017), the Court of Appeals for the Fifth Circuit described two distinct bases for compelling arbitration with respect to non-signatories: the "intertwined claims" theory and the "direct benefits" theory. The intertwined claims theory governs motions to compel arbitration when a signatory plaintiff brings an action against a non-signatory defendant asserting claims dependent on a contract that includes an arbitration agreement that the defendant did not sign. The direct benefits theory of equitable estoppel prevents a non-signatory from knowingly exploiting an agreement containing the arbitration clause. That theory serves to prevent a non-signatory from suing under an agreement while at the same time seeking to avoid its arbitration clause. For a recent decision, discussing in both the majority and dissenting opinions the direct benefits estoppel theory, in ERISA cases, see, e.g., Cooper v. Ruane Cunniff & Goldfarb Inc., 990 F.3d 173 (2d Cir. 2021) and Torres v. Starbucks Corp., 2021 U.S. Dist. LEXIS 47821 (M.D. Fla. 2021) (for failure to provide a compliant COBRA notice, discussing estoppel theory, and also holding that third-party beneficiary not applicable when plaintiff is not bringing an action on the contract).

Arbitration of Class Actions Claims

Two recent Supreme Court cases provide important background for the recent ERISA litigation surrounding the enforceability of class action waivers. In Epic Systems Corp. v. Lewis, 138 S. Ct. 1622 (2019), the Supreme Court held that mandatory arbitration agreements, that included class and collective action waivers, did not violate Section 7 of the National Labor Relations Act, were enforceable according to their terms, and could only be invalidated subject to traditional contract defenses.

However, while the *Epic Systems* decision is significant precedent establishing that class action claims that allege statutory violations of law can be individually arbitrated, shortly thereafter, the Supreme Court provided an important caveat to Epic Systems in Lamps Plus, Inc. v. Varela, 139 S. Ct. 1407 (2019). In *Lamps Plus*, the Supreme Court clarified that "[c]lass arbitration is not only markedly different from the 'traditional individualized arbitration' contemplated by the FAA, it also undermines the most important benefits of that familiar form of arbitration"' Lamps Plus, Inc, 139 S. Ct. at 1415. This was the first Supreme Court decision in a decade that, from a policy perspective, did not emphasize the benefits of arbitrating class action disputes and as a result, made it more difficult to arbitrate class claims. The Court specifically said that, for a class action arbitration agreement to be legally enforceable, there must be unambiguous and affirmative consent to subject class action claims to arbitration. Lamps Plus, Inc., 139 S. Ct. at 1416. In reaching this decision, in not allowing an agreement to waive class action litigation rights to be inferred, the Court noted that the policy advantages of arbitration are lacking in the context of class actions, explaining that a class action "sacrifices the

principal advantage of arbitration-its informality-and makes the process slower, more costly, and more likely to generate procedural morass than final judgment." Lamps Plus, Inc., 139 S. Ct. at 1416.

Arbitration in ERISA Plan Claim Review Procedures

ERISA plans must provide for internal benefit claim review and appeal procedures that are designed to ensure, among other things, a reasonable opportunity to obtain a full and fair review of any decision to deny benefits sought under the plan. The implementing regulations establish minimum standards for these internal procedures. For checklists that enumerate the regulatory requirements for ERISA plan claims review procedures, see Claims Procedure ERISA Requirements Checklist (General Rules), Claims Procedure ERISA Requirements Checklist (Group Health Plans) and Claims Procedure ERISA Requirements Checklist (Disability Benefits).

The regulations do not preclude the use of arbitration as part of a compliant review process, so long as it satisfies the regulatory standards. However, one rule also clarifies that a group health plan or a disability plan may only impose mandatory arbitration for a required level of review if (1) the arbitration is conducted in accordance with the requirements of the claims review procedure regulations applicable to such appeals and (2) the claimant is not precluded from challenging the arbitrator's decision in court under ERISA Section 502(a) (29 U.S.C. § 1132(a)) or other applicable law. 29 C.F.R. § 2560.503-1(c)(4).

In Sanzone-Ortiz v. Aetna Health of Cal., Inc., 2015 U.S. Dist. LEXIS 171624 (N.D. Cal. 2015) and 2016 U.S. Dist. LEXIS 113252 (N.D. Cal. 2016), the district court held that an insurer's mandatory arbitration provision did not violate 29 C.F.R. § 2560.503-1(c)(4) because that regulation did not govern proceedings following a plan's final determination. The court further concluded that even if the regulation could be read as prohibiting mandatory arbitration, the DOL regulation was not based upon a "Congressional command" that would override the Federal Arbitration Act's mandate favoring arbitration agreements.

It is noteworthy that 29 C.F.R. § 2560.503-1(c)(4) does not speak to the enforceability of voluntary arbitration agreements negotiated separately by parties outside of the plan itself. Mem'l Hermann Hosp. Sys. v. Unicare Health Plans of Tex., 2011 U.S. Dist. LEXIS 171434 (S.D. Tex. 2011).

Arbitration for Voluntary Level of Review

The DOL regulations also recognize that an additional voluntary level of appeal can use a binding arbitration process, provided that certain requirements are met, including furnishing a claimant with sufficient information about the plan's voluntary process to permit the participant to make an informed decision about whether to submit the dispute to arbitration. 29 C.F.R. § 2560.503-1(c)(3)(iv). This requirement includes information about the applicable rules, the process for selecting the decision maker, and the circumstances, if any, that may affect the impartiality of the arbitrator, such as having any personal or financial interests in the result or any past or present relationship with any party to the review process. The retirement plan also must make clear to the claimant that any decision as to whether to submit a dispute to the voluntary level of appeal will have no effect upon the claimant's rights to any other benefits under the plan.

The DOL instructs that 29 C.F.R. § 2560.503-1(c)(3) includes two protections designed to ensure that any additional appeal level offered by the plan remains purely voluntary and does not adversely affect the claimant:

- First, subparagraph(c)(3)(i) requires any plan offering a voluntary appeal to agree not to later assert a defense of failure to exhaust administrative remedies against a claimant who chooses not to make use of the voluntary appeal process.
- Second, subparagraph (c)(3)(ii) requires plans offering voluntary levels of appeal to agree that any defense based upon a statute of limitations or other defense based upon timeliness is tolled while the dispute is under submission to the voluntary appeals process. 29 C.F.R. § 2560.503-1(c)(3)(i).

65 Fed. Reg. 70,246, 70,253–54 (Nov. 21, 2000).

While the preamble to the final 2000 claims review procedure regulations indicates that the focus of the voluntary appeal provisions is to protect claimants, in Snyder v. Fed. Ins. Co., 2009 U.S. Dist. LEXIS 20225 (S.D. Ohio 2009), the district court held that arbitration is voluntary for both parties, and if an insurer did not agree to arbitration, plaintiff could not mandate the arbitration. Other cases have held that plan provisions that are inconsistent with 29 C.F.R. § 2560.503-1(c)(4) will not be enforced. Sosa v. Parco Oilfield Servs., 2006 U.S. Dist. LEXIS 70312 (E.D. Tex. 2006) and Williams v. Ass'n de Prevoyance Interentreprises, 2012 U.S. Dist. LEXIS 68488 (E.D. La. 2012) (Forcing a plaintiff to travel to France and initiate arbitration at his expense is unreasonable and unenforceable.).

Arbitration of Statutory ERISA Claims

Most Circuit Courts of Appeal have expressly held that arbitration agreements that cover legal rights to bring claims pursuant to alleged statutory violations of ERISA are enforceable:

- Bird v. Shearson Lehman/American Express, Inc., 926 F.2d. 116 (2d Cir. 1991), cert. denied, 501 U.S. 1251 (1991)
- Pritzker v. Merrill Lynch Pierce Fenner & Smith, 7 F.3d 1110 (3d Cir. 1993)
- Kramer v. Smith Barney, 80 F.3d 1080 (5th Cir. 1996)
- Smith v. Bd. of Dirs. of Triad Mfg., 13 F.4th 613 (7th Cir. 2021)
- Arnulfo P. Sulit v. Dean Witter Reynolds, 847 F.2d 475 (8th Cir. 1998)
- Dorman v. Charles Schwab, 780 Fed. Appx. 510 (9th Cir. 2019)
- Williams v. Imhoff, 203 F.3d 758 (10th Cir. 2000)

The Sixth Circuit, without ruling on the issue, noted that: "every other circuit to consider the issue has held that "ERISA [statutory] claims are generally arbitrable." Hawkins v. Cintas Corp., 32 F.4th 625, 629 (6th Cir. 2022) quoting Smith v. Bd. of Dirs. of Triad Mfg., Inc., 13 F.4th 613, 620 (7th Cir. 2021) (collecting cases from the Second, Third, Fifth, Eighth, Ninth, and Tenth Circuits). It is therefore widely accepted that arbitration provisions in ERISA plans are permissible and enforceable against potential claims alleging ERISA statutory violations.

Even though it is nearly uniformly accepted that ERISA claims are arbitrable, there has been recent litigation concerning whether breach of fiduciary claims specifically alleging violations of ERISA Section 502(a)(2) (29 U.S.C. § 1132(a)(2)) are arbitrable, as discussed below in greater detail. Litigation has typically focused on two separate issues: (1) whether an ERISA plan can agree to arbitrate when ERISA Section 502(a)(2) claims are brought by participants in a representative capacity on behalf of a plan and (2) if it can be established there was an agreement to arbitrate, whether the "effective vindication" exception, discussed above, precludes the arbitration of breach of fiduciary claims brought on behalf of the plan.

The first issue concerns whether an ERISA plan can agree to arbitrate ERISA Section 502(a)(2) breach of fiduciary claims that are brought by plan participants in a representative capacity on behalf of an ERISA plan. Demonstrating an agreement to arbitrate exists is a necessary element to compel arbitration. Therefore, if an ERISA plan participant brings claims on behalf of an ERISA plan but it is determined that the plan has not agreed to arbitrate those claims, arbitration cannot be compelled against the plan. This was the Sixth Circuit's reasoning in the *Cintas* case. The Sixth Circuit held that agreements to arbitrate in employment agreements that required employees to agree to arbitrate all claims that either the employee or employer has against the other party could not bind the *plan* to arbitration of a breach of fiduciary duty claims brought by participants on behalf of the plan. 32 F.4th 625, 631 (6th Cir. 2022). The Sixth Circuit specifically ruled that ERISA participants' claims brought in a representative capacity on behalf of an ERISA plan pursuant to ERISA Section 502(a)(2), could not be waived by an individual arbitration agreement, because the claims were being brought by participants on behalf of the plan, and a participant could not waive the plan's rights to relief through an employment agreement.

In another important decision, in *Cooper*, the Second Circuit ruled that an arbitration clause in an employment agreement stating that the employee agreed to arbitrate "all legal claims arising out of or relating to employment" did not encompass ERISA Section 502(a)(2) claims. 990 F.3d at 184. Notably, the arbitration clause of the employment agreement specifically excluded ERISA-related benefits provided under a Company sponsored benefit plan. The Second Circuit reasoned that because (i) the facts underlying the claim *e.g.* the investment decisions made by the ERISA plan in question did not relate to the plaintiff's employment and (ii) other persons/entities had statutory standing to bring a claim under 502(a)(2) other than employees of the sponsor, there was no agreement to arbitrate pursuant to the language "relating to employment." *Id.*

In contrast to agreements to arbitrate contained in employment agreements, courts have typically found that participants of ERISA plans implicitly agree to arbitrate the scope of ERISA claims set forth in an ERISA plan arbitration provision through their participation in the particular plan. Dorman, 780 F. App'x at 513.

In an interesting decision that bucks the trend, however, the U.S. District Court for the Western District of Kentucky, recently held that participants of an ESOP did not agree to an arbitration provision in the plan document because no evidence was submitted that they were "on notice" of the agreement to arbitrate. Best et al. v. James et al., No. 3:20-CV-299-RGJ, 2022 U.S. Dist. LEXIS 171462 at *3 (W.D. Ky. Sept. 22, 2022). But the court held that the

participants' claims were precluded anyway by arbitration in the plaintiffs' and the class members' employment agreements. Id. Notably, unlike the claims in Cintas, the plaintiffs in Best brought claims on behalf of other participants but not the plan itself.

This decision has been appealed to the Supreme Court. As of the date of publishing, the Supreme Court has asked plaintiffs in the matter to respond to the writ of certiorari but has not ruled yet in accepting the appeal.

The second issue concerns whether an agreement to arbitrate an ERISA § 502(a)(2) claim meets the so-called effective vindication exception set forth by the Supreme Court in *Italian Colors*. As discussed above, the Seventh Circuit in *Smith* applied *Italian Colors* to hold that the arbitration agreement in question would impermissibly shut the door to the effective vindication of an ERISA plan participant's statutory rights to bring a representative ERISA Section 502 (a)(2) cause of action to remove and replace a plan fiduciary. Smith, 13 F.4th 613, 621 (7th Cir. 2021). This is an important decision whose application has, and will likely continue to be, duked out in District Courts.

For some context, ERISA Section 502(a)(2) expressly allows claims to enforce ERISA § 409 (29 U.S.C. § 1109), which provides that a breaching fiduciary is personally liable to make good to a plan for any losses resulting from the breach. In Italian Colors Rest., 570 U.S. 228 (2013), discussed above, the Supreme Court recognized that the *dicta* in the decision in Mitsubishi Motors Corp v. Soler Chrysler Plymouth, Inc., 471 U.S. 614, 637 (1985),suggests the possibility of invalidating, on public policy grounds, arbitration agreements that prevent plaintiffs from effectively vindicating their rights under federal law. This has been termed the "effective vindication exception." The Supreme Court has not invalidated an arbitration agreement on this ground. But the Seventh Circuit in *Smith* did so because it determined: (a) the arbitration provision of the plan document in question banned representative and group lawsuits that seek plan-wide remedies on behalf of other participants; (b) the participants alleged equitable relief on behalf of the plan pursuant to Section 502(a)(2), specifically the removal of the plan trustee and the appointment of a new fiduciary; (c) such alleged relief has plan-wide effect effectively banned by the arbitration provision and (d) therefore, individualized arbitration of plaintiff's claim would impermissibly foreclose the plaintiff from obtaining relief available to him under ERISA Section 502(a)(2).

The Seventh Circuit noted, however, that the decision was strictly limited to the specific claims alleged, the relief sought, and the specific arbitration provision in question and in so doing, encouraged District Courts to make fact specific determinations without applying bright-line rules about the availability of the effective vindication exception.

Accordingly, the application of the *Smith* holding, and the scope of its ruling has been, and will be, tested moving forward by new litigation. In just the short time since the *Smith* holding, Courts have distinguished *Smith* based upon the substance of the arbitration agreement in question. For example, in Holmes v. Baptist Health S. Fla., Inc., No. 21-22986, 2022 U.S. Dist. LEXIS 10834, at *7 (S.D. Fla. Jan. 20, 2022), the Southern District of Florida determined that the arbitration clause in the plan that covered claims arising out of, or concerning the plan, that seek "remedial or equitable relief" or provide for "additional benefits or monetary relief to any person" was binding and enforceable and subjected plaintiffs' claims (brought on behalf of the plan) to arbitration. Interestingly, like in *Smith*, the plaintiffs alleged the removal of fiduciaries and the appointment of new fiduciaries but the District Court held that the plaintiffs had expressly waived the right to bring a class action through the plan's arbitration provision and even if they had not, the arbitration provision in question did not expressly bar the relief sought like it did in *Smith*. This result though can be contrasted with a recent case in the District of Colorado, Harrison v. Envision Mgmt. Holding, Inc., No. 21-cv-0304-RMR-NYW, 2022 U.S. Dist. LEXIS 60823, at *12 (D. Colo. Mar. 24, 2022) where the court held that the arbitration agreement in question prevented the removal and replacement of fiduciaries and therefore, the district court found that because the plan precluded the plaintiff from seeking plan-wide remedies, the plaintiff could not effectively vindicate his ERISA rights.

In reconciling these two outcomes, the District Court in Arizona reviewed all of the pertinent case law and concluded that case law does not establish that a "plaintiff has an unqualified right to bring a collective action to recoup losses" and therefore the effective vindication exception can only be triggered where "a provision in an ERISA plan precludes an individual participant from pursuing equitable remedies, such as removal of a fiduciary, that would benefit other participants." Robertson v. Argent Tr. Co., No. CV-21-01711-PHX-DWL, 2022 U.S. Dist. LEXIS 133578, at *28-29 (D. Ariz. July 27, 2022).

Given the disparate outcomes and the fact specific nature of the holdings it is likely that continued litigation on the effective vindication exception will continue.

For a treatise discussion of arbitration in the Third Circuit, see, Arbitration - The Third Circuit Re-Examines Its Traditional Approach to Adjudication of ERISA Claims. Pritzker v. Merrill Lynch, Pierce, Fenner & Smith, Inc. (1993), 39 Vill. L. Rev. 957.

Note, however, that in Gaffers v. Kelly Services, Inc., 900 F.3d 293, 296 (6th Cir. 2018), the Court of Appeals for the Sixth Circuit held that employees can, through collective bargaining, choose arbitration as the forum within which to resolve federal claims.

Arbitration in Employment Agreements versus Plan Documents

As discussed above, several courts have ruled recently that With respect to class action waivers and mandatory arbitration provisions contained in employment agreements rather than plans are unenforceable because the plan itself did not agree to the agreement not to arbitrate.; , several courts have followed the decision of the Ninth Circuit in Munro v. University of Southern California, 896 F.3d 1088 (9th Cir. 2018); . See also Hawkins, v. Cintas Corps., 2021 U.S. Dist. LEXIS 14766 (S.D. Ohio January 2021); 32 F.4th at 631; Ramos v. Natures Image, Inc., 2020 U.S. Dist. LEXIS 88181 (C.D. Cal. 2020). In contrast to an employment agreement between a plan sponsor and an individual employee, an ERISA plan document is by definition the contract (unilateral in nature except for multiemployer plans) between the plan and all of its participants and therefore have a greater effect. In Dorman v. The Charles Schwab Corporation, 780 Fed. Appx. 510 (9th Cir. 2019), the Court of Appeals for the Ninth Circuit, in a controversial decision, held that a plan can consent to arbitrate ERISA Section 502(a)(2) claims that a plan participant may bring derivatively through an arbitration provision contained in the plan document. It is unclear whether Dorman will be followed in other Circuit Courts of Appeals. However, a recent Northern District of Illinois decision, for example, concluded that Section 502(a)(2) belongs to the plan itself, and cannot be subjected to mandatory arbitration by virtue of the arbitration provision existing in a plan document. Smith v. GreatBanc Trust Co., 2020 U.S. Dist. LEXIS 151992 (N.D. Ill. 2020). The Smith court stated in emphatic terms that: "the Plan Document was executed unilaterally by the plan sponsor. . . . A plan document drafted by fiduciaries – the very people whose actions have been called into question by the lawsuit - should not prevent plan participants and beneficiaries from vindicating their rights in court." Id. citing Dorman v. Charles Schwab & Co., 2018 U.S. Dist. LEXIS 9107, at *14 (N.D. Cal. 2018) (emphasis added). The District Court further surmised that "allowing the fiduciary to unilaterally require plan participants to arbitrate claims for breach of fiduciary duty would, in a sense, be allowing the fox to guard the henhouse." Id. quoting Brown v. Wilmington Trust, N.A., 2018 U.S. Dist. LEXIS 123690, at *5 (S.D. Ohio 2018). The Smith decision as of the publication of this article is currently pending an appeal to the Seventh Circuit. Smith v. Board of Directors of Triad Manufacturing Inc., et al, No. 20-2708 (7th Cir. 2021).

Arbitration Provisions Added after Participant's Termination of Employment

Participants have successfully challenged the enforceability of arbitration provisions and/or class action waivers which were added to the plan document after the participant had ceased participation in the plan, based in part upon contract law principles of mutual consent. For example, in Brown v. Wilmington Trust, N.A., 2018 U.S. Dist. LEXIS 123690 (S.D. Ohio July 24, 2018), the district court held that a former ESOP participant was not bound by an ERISA plan's mandatory arbitration provisions and class action waiver because:

- Those plan provisions were added to the plan when she was no longer an ESOP participant –and–
- Her claim for fiduciary duty accrued when she was a participant in the plan, and the arbitration provisions were not in effect
    - Under similar facts, courts have found arbitration provisions that were added to plan documents after participants left the plan to be unenforceable. See, e.g., Coleman v. Reliance Trust Co., 2019 U.S. Dist. LEXIS 223195 (E.D. Tex. 2019); Smith v. GreatBanc Trust Co., 2020 US Dist. LEXIS 151992 (N.D. Ill. 2020); and Hensiek v. Bd. of Dirs. of Casino Queen Holding Co., 2021 U.S. Dist. LEXIS 17954 (S.D. Ill. 2021).

While it is clear that adding an arbitration provision to a plan document after an individual ceases to be a plan participant does not bind the former participant to arbitration, it is an open issue whether arbitration applies to a situation in which the ERISA cause of action accrues during a time period when the arbitration provision was not in effect.

The Particular Question of Arbitration of Section 502(a)(2) Claims

As noted above, arbitration provisions may be unenforceable where there exists a contrary Congressional command such that enforcing an arbitration provision would preclude the effective vindication of statutory rights. In the context of claims made pursuant to ERISA § 502(a)(2) (29 U.S.C. § 1132(a)(2)), which expressly permits claims seeking plan-wide remedies for fiduciary breaches. The

determination of whether this statutory right constitutes such a contrary Congressional command that could render an arbitration provision unenforceable for a defined contribution plan depends upon whether participants in such a plan have an unequivocal right to pursue relief on behalf of the plan as opposed to the individualized relief that they could secure in arbitration. Resolution of this issue depends upon the manner in which courts interpret the Supreme Court's decision in LaRue v. DeWoll, Roberg & Associates, Inc., 473 U.S. 134 (1985), a matter on which courts have differed.

In *LaRue*, the Supreme Court clarified that its holding in *Massachusetts Mutual Life Ins. Co. v. Russell*, which limited recovery under ERISA Section 502(a)(2) exclusively to injuries to an ERISA retirement plan, not an individual participant, did not extend to participants in defined contribution retirement plans. In *LaRue*, the Supreme Court stated that "[w]hether a fiduciary breach diminishes plan assets payable to all participants and beneficiaries, or only to persons tied to particular individual accounts, it creates the kind of harms that concerned Section 409's draftsmen." LaRue, 473 U.S. at 2 (ERISA Section 409, which is cross-referenced in Section 502(a)(2), provides that a breaching fiduciary is personally liable to make good to the plan for any losses incurred)..

The *Dorman* court seized upon this distinction drawn in *LaRue* to conclude that, in the case of defined contribution plans, the relief available under ERISA Section 502(a)(2) is "inherently individualized." Dorman, 780 Fed. Appx. 510, at *6. However, the district court in *Smith* disagreed with the Ninth Circuit's interpretation of *LaRue* because "[t]he Supreme Court did not indicate in LaRue that Section 502(a)(2) claims are inherently individualized, nor did it suggest that an individual plan participant's claim can somehow be split from a claim seeking plan wide relief." Smith, 2020 U.S. Dist. LEXIS 151992, at *14.

Note that the *Smith* case is on appeal to the Seventh Circuit. A decision approving *Smith* would create a clear conflict between the circuits, which could result in the Supreme Court's addressing the issue.

As discussed above, on appeal, while the Seventh Circuit was careful to limit its decision to the particular arbitration agreement in question, it is likely that litigation will ensue regarding whether the arbitration agreement of the plan would forbid the equitable relief promised to participants pursuant to ERISA § 409 and in turn, what are the substantive rights participants possess under ERISA Section 409.

Advantages and Disadvantages of Mandatory Individualized Arbitration

There are advantages and disadvantages to drafting an employee benefit plan or employment agreement to mandate individualized arbitration, as discussed below.

Disadvantages of Implementing Mandatory Arbitration

There are several disadvantages to mandating arbitration.

Inconsistent Arbitration Decisions

Perhaps the primary negative of individualized arbitration, and perhaps the most likely to occur, is the possibility of inconsistent determinations by different arbitrators. By way of example, one arbitrator might determine that plan recordkeeping or investment management fees are excessive, while a second arbitrator might determinate that they are reasonable in nature. A plan sponsor facing many individualized arbitrations from multiple participants alleging the same misconduct may therefore find itself in the position of receiving inconsistent and contradictory rulings regarding the prudence of its plan design, structure, administration, and investment policy. Inconsistent and/or contradictory arbitration rulings could cause confusion as to whether the plan is being administered in a lawful fashion. This lack of determinative guidance could cause confusion concerning a plan's compliance with ERISA's fiduciary duties. It is also important to note that the DOL is empowered to bring breach of fiduciary claims against ERISA plans and an arbitration decision would not be of assistance in protecting against such potential litigation or enforcement action.

Discrete Tax Qualification Concerns

A blanket mandatory arbitration clause could pose tax qualification concerns in the context of meeting IRS requirements regarding nondiscrimination rules. Revenue Ruling 2002-45, 2002-2 C.B. 116, addresses various contributions to tax-qualified defined contribution plans by plan sponsors or third parties, including nondiscrimination testing under the I.R.C. Section 401(a)(4) and the maximum annual allocation of contributions under I.R.C. Section 415. In that ruling, the IRS held that if a payment made to a qualified defined contribution plan is made to restore losses to the plan resulting from actions by a fiduciary for which there is a reasonable risk of liability for breach of a fiduciary

duty under Title I of ERISA and plan participants who are similarly situated are treated similarly with respect to the payment, the payment will not be treated as a contribution to the plan, and therefore would not be tested under the applicable nondiscrimination rules.

Both the Revenue Ruling and the regulations under I.R.C. Section 415, which incorporates the provisions of Revenue Ruling 2002-45, refer to such payments as restorative payments. Breaches of fiduciary duty referenced in these IRS pronouncements would not include those relating to a tax qualification requirement, such as a breach of fiduciary duty resulting from a failure to remit contributions to the plan. Restorative payments would include payments made pursuant to a DOL order, the DOL's Voluntary Fiduciary Correction Program, or a court-approved settlement, and should also include arbitration awards or settlements.

While the determination of whether a payment to a qualified defined contribution plan is treated as a restorative payment rather than a contribution is based upon all of the relevant facts and circumstances, the IRS reiterated later in Revenue Ruling 2002-45 that "payments that result in different treatment for similarly situated plan participants" are not restorative payments. Similarly situated plan participants are not defined for this purpose, but it will clearly be difficult in most instances to take the position that plan participants who requested arbitration are not similarly situated to those who do not request arbitration.

As a result, if the individuals receiving favorable results in arbitration are highly compensated employees under I.R.C. Section 414(q), then I.R.C. Section 410(b) will be violated. This is because the plan sponsor will be maintaining a plan with only highly compensated employees. If favorable results in arbitration are received by some highly compensated employees and some non-highly compensated employees, it may be possible to satisfy Section 410(b) relying upon the demographics of the group receiving favorable awards in arbitration. But, at a minimum, nondiscrimination testing will be required under Section 401(a)(4), because even if the plan participants are successful in arbitration, the amounts of their awards may vary, so satisfaction of Treasury Regulation safe harbors under Section 401(a)(4) for defined contribution plans will not be available. With respect to I.R.C. Section 415, Treasury Regulation Section 1.415(c)-1(b)(2)(ii)(C) contains the same language as Revenue Rule 2002-45, so arbitration payments that are not made to similarly situated participants would be taken into account for purposes of determining the maximum permissible allocation.

Duty of Impartiality

A subset of the duty of loyalty under ERISA is the duty of impartiality. Endries v. Bd. of Dirs. of the Motion Picture Indus. Health Plan, 2020 U.S. Dist. LEXIS 199264 (C.D. Cal. 2020). In Morse v. Stanley, 732 F.2d 1139 (1984), the Second Circuit Court of Appeals stated that trustees owe a duty to act impartially with plan participants and retired beneficiaries and/or their families and the trustee must deal even-handedly among them and do its best to have the entire trust looked at as a whole. Similarly, in Varity Corp. v. Howe, the Supreme Court stated that "the common law of trusts . . . requires a trustee to take impartial account of the interest of all beneficiaries." 516 U.S. 489, 514 (1996). At common law, the duty of impartiality was applied most often to protect the interests of successive beneficiaries, for example, income and principal beneficiaries, but the duty also applies where trustee is required to act impartially vis-à-vis, beneficiaries with present interests. Jackson v. Truck Drivers Union Local 42 Health and Welfare Fund, 933 F. Supp. 1124, 1144 (D. Mass. 1996). It is difficult to reconcile this duty with the potential differing treatment of similarly situated plan participants in individualized arbitration. The consequences of breaching this fiduciary duty could expose the plan to potential enforcement action or litigation involving the DOL.

Arbitration's Lack of Preclusive and Precedential Effects Decisions

Several individualized arbitrations of claims arising from the same misconduct would not have the same, or perhaps any, preclusive or precedential effects. Therefore, if the plan prevails in one arbitration against a participant, it would not preclude another participant from bringing the same claim and hoping for a better result with a different arbitrator. This could force the plan sponsor to defend many individualized arbitrations of the same misconduct repeatedly, particularly in the instance of a large class action claim where there could be hundreds of individualized claims. Hundreds of potentially different decisions with different reasonings could also result in confusion regarding interpretation of plan terms without a singular judicial precedent for plan fiduciaries to rely on. For example, ERISA Section 404(a)(1)(D) requires a fiduciary to "discharge his/her duties with respect to a plan in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with ERISA." But if, for example, an arbitrator's determination is that an item was improperly excluded from a participant's pensionable earnings under the plan and arbitrations produced inconsistent results, it would be difficult for a plan administrator to deal with those inconsistent results in a streamlined fashion to comply with his or her duties under ERISA Section 404(a)(1)(D).

Perceived Unfairness to ERISA Plan Participants

Whether expressed as a concern for fairness or rule of law values such as uniformity, predictability, and certainty, it is important for participants that they be treated in equivalent fashion. If a plan participant receives an unanticipated adjustment to his or her benefit, he or she is likely to ask other plan participants if they received similar treatment. Unequal treatment of participants in this fashion is obviously a lesser level of concern than plan disqualification or breach of fiduciary duty, but the inconsistent treatment of plan participants may have a negative effect upon the manner in which plan participants view the plan.

Arbitrators May Be Unfamiliar with ERISA Rules, Regulations, and Case Law and Arbitration Decisions Cannot Be Appealed Like Judicial Decisions

ERISA is a very complicated body of law that involves many interrelated legal duties, rules, and regulations. Many judges have had years of experience analyzing ERISA claims, particularly breach of fiduciary claims, with repeated opportunities to issue legal opinions on the subject. In contrast, arbitrators may not have any familiarity at all with ERISA, let alone any experience interpretation the meaning of ERISA rules, regulations, and legal duties. This unfamiliarity with ERISA could put the plan sponsor at the mercy of an unreasonable binding arbitration decision that cannot be appealed in the same fashion as a judicial decision, which affords opportunities to make motions for reconsideration and appeal a decision deemed unreasonable to an appellate court.

Aside from these noted points, below are additional bullet points potential disadvantages to arbitration:

- Arbitration is not always less expensive than litigation. Parties must pay the tribunal their fees and any disbursements plus any administrative costs (e.g., administrative fees to the arbitral institution that is administering the arbitration), which may be substantial when compared with the cost of court proceedings.
- Class action litigation, while often costly, may have advantages for plan sponsors. Specifically, defendants may prefer to resolve all potential disputes arising out of the same facts and circumstances in one forum, rather than addressing multiple individual participant claims in serial arbitration proceedings. At a minimum, aside from the possibility of inconsistent determinations, mass filings of arbitration claims are simply inefficient.
- With respect to run of the mill non-fiduciary claims, providing for mandatory arbitration, rather than allowing for civil litigation to resolve a participant's claims, might encourage a plan participant who had received an adverse benefit determination and who would be unlikely to initiate litigation to request review by arbitration.

Finally, as we mentioned above, an arbitrator's decision might not have the same binding effect as a court opinion on an agency auditing the plan, such as the DOL.

Advantages to Mandatory Individual Arbitration

And, as expected, several advantages exist to mandating arbitration.

Cost Savings

Defending against a class action particularly against an ERISA class action, may involve hundreds if not thousands of hours of attorney work if the litigation cannot be disposed of at the motion to dismiss stage. The amount of attorney work, the sophistication of the work, and the need for the retention of expert witnesses can result in millions of dollars in legal fees. As one glaring example, in the ERISA litigation, **Tussey v. ABB**, defense counsel for ABB and Fidelity received $42 million in fees, according to a court filing in that case. See National Association of Plan Advisors, Schlichter Settlement Highlights the Cost of Litigation (Aug. 20, 2019).

Efficiency and Speed

In the event litigation is not settled or dismissed at a nascent stage, fact and expert discovery can last several years prior to a court's final disposition at the summary judgment stage or during a bench trial. Any decision can thereafter be appealed to an appellate court. Therefore, the dispute has the potential to last many years before a final and binding determination is made. The *Tussey v. ABB* case is again instructive in this regard as the litigation lasted over 12 years and involved nearly 30,000 hours of plaintiff counsel's claimed attorney work. See Benefits Pro, Law Firms Received More than $50 Million for Tussey vs. ABB (Dec. 28, 2015). Arbitration, which has an abbreviated discovery process, would result in a much quicker and efficient determination of an ERISA claim.

Deterrent to Plaintiff Lawyers

As discussed above, there has been an exponential rise in the amount of ERISA class breach of fiduciary duty action claims filed in recent years. This rise may partly be explained by favorable case law that has developed in many Circuit Courts of Appeals that provides very lenient legal standards to:

- Plead a plausible fiduciary breach claim –and–
- Certify classes of similarly situated participants
    - It may also be explained by many large settlements paid to plaintiff's counsel.

In 2020 alone, the top 10 ERISA class action settlements totaled $380.10 million which topped the 2019 total of $376.35 million, as well as the 2018 total of $313.4 million. See Seyfarth, Workplace Class Action Litigation Report (Jan. 5, 2021). Because plaintiff lawyers are strongly incentivized to bring class actions to receive a lucrative continency fee based upon the potential size of a class action settlement, limiting relief under the terms of a plan to separate and individualized arbitration could serve as a deterrent to protect against potential suits.

Arbitrators Are Not Bound to Judicial Precedent

Arbitrators are not bound to judicial precedent and therefore the proceedings can allow for more room for negotiation and opportunities to settle with a participant and reach middle ground. This flexibility is especially important considering several jurisdictions currently have plaintiff friendly case law, specifically at the pleading stage.

Discovery Is Abbreviated and Limited

Discovery is more limited in arbitration than in litigation and the amount of discovery to be exchanged is within the discretion of the arbitrator. Therefore, the burdens and expense associated with traditional judicial discovery could be avoided. It is important to note though that with respect to judicial review of benefit claim denials, in most instances the determination is made on the administrative record.

Arbitration Does Not Take Place in Public

Arbitration is generally private in the sense that hearings are not held in a public courtroom and there is no public docket. This benefit is important for the plan sponsor to avoid any negative publicity associated with litigation of an ERISA claim.

Arbitrators May Be Friendly to Plan Sponsors

Arbitrators might have built in bias towards plan sponsors because plan sponsors pay their fees as opposed to bias towards individual participants.

Multiemployer Withdrawal Liability Arbitration

Under ERISA Section 4221, any dispute between an employer and plan sponsor concerning any determination made with respect to multiemployer withdrawal liability must be resolved through arbitration. Either party may request arbitration within the 60-day period beginning before the earlier of:

- The date of the plan's response to the employer's request for review –or–
- 120 days after the employer's request for review

The parties may also jointly request arbitration within the 180-day period after the plan's initial demand letter to the employer assessing withdrawal liability. A party that unilaterally initiates arbitration is responsible for establishing that notice of the initiation of arbitration was timely received by the other party. PBGC Regulation 4221.3(c). The contents of the notice vary depending upon whether arbitration is being initiated by the employer or another party. 29 C.F.R. § 4221.3(d).

The parties may agree at any time to extend or waive the time limits for initiating arbitration. 29 C.F.R. § 4221.3(b).

The parties are required to select the arbitrator within 45 days after the arbitration is initiated, or such other period as mutually agreed to by the parties. The arbitrator's appointment becomes effective upon his or her written acceptance, stating his or her availability to service. If the arbitrator does not accept in writing within 15 days after the notice of appointment is mailed or delivered, he or she is deemed to have declined the appointment, and the parties must select a new arbitrator.

Upon accepting the appointment, the arbitrator is required to disclose to the parties any circumstances likely to affect his or her impartiality, including any bias or personal or financial interest that he or she may have in the matter, or any past or present relationship with the parties or their counsel. If a party determines that, based upon the disclosed information, the arbitrator should be disqualified, the party must notify the other party and the arbitrator within 10 days after the arbitrator makes the disclosure but in no event after the arbitration hearing has begun. Under these circumstances, the parties will again select an arbitrator.

After the arbitrator has been selected, a party may request that he or she withdraw from the proceedings at any time before a final award is rendered on the ground that he or she is unable to issue an award impartially. The request for withdrawal shall include a statement of the circumstances that, in the opinion of the requesting party, affect the arbitrator's impartiality and a statement that the requesting party has brought these matters to the attention of the arbitrator and the other parties at the earliest possible stage of the proceedings. If the arbitrator agrees that the circumstances are likely to affect his or her impartiality, he or she shall notify the parties and withdraw from the proceedings. The parties will then select a new arbitrator within 20 days after notice of the withdrawal.

Replacing an Arbitrator

The newly appointed arbitrator rehearing the matter may, in his or her discretion, rely upon the record already established.

The 20-day period for replacing an arbitrator who withdraws is equally applicable if filling a vacancy resulting from the arbitrator's disqualification, resignation, death, or inability to perform his or her duties at any time before a final award is rendered.

Procedure

In rendering his or her decision, the arbitrator is required to follow applicable law with respect to ERISA. The arbitrator may allow a party to conduct prehearing discovery. The arbitrator judges the admissibility of evidence, and conformity to legal rules is not required. Prehearing conferences may be appropriate and if the parties agree an award may be issued without a hearing. The rules governing the conduct of these arbitration hearings is set forth in 29 C.F.R. § 4221.6.

If the parties have not provided for the cost of the arbitration, including the arbitrator's fees, by agreement, the arbitrator is authorized to assess such fees. The PBGC regulations provide that each party to a dispute shall pay the costs of its own witnesses, and if only one party requests a transcript of a hearing, that party must pay for it. The default rules are that other costs of the arbitration be shared equally by the parties. The arbitrator may award reasonable attorney's fees, but regulations provide that such fees should only be awarded if a party initiates or contests an arbitration in bad faith or engages in dilatory, harassing, or other improper conduct during the course of the arbitration. 29 C.F.R. § 4221.10.

Any determination made by the plan sponsor of the multiemployer plan with respect to withdrawal liability is presumed correct unless the party contesting the determination shows by a preponderance of the evidence that the determination was unreasonable or clearly erroneous. With respect to determinations of a plan's unfunded vested benefits for a plan year, the determination is presumed correct unless the party challenging the determination shows by a preponderance of the evidence that either the actuarial assumptions and methods used in the determination were, in the aggregate, unreasonable (taking into account the experience of the plan and reasonable expectations), or the plan's actuary makes a significant error in applying the actuarial assumptions or methods.

There is a presumption, rebuttable only by a clear preponderance of the evidence, that the findings of fact made by the arbitrator are correct.

In lieu of the rules for conducting an arbitration set forth in PBGC regulations, PBGC Regulation permits an arbitration to be conducted in accordance with an alternative procedure approved by the PBGC. A plan may, by plan amendment require the use of a PBGC-approved procedure in all arbitrations of withdrawal liability disputes, or the parties may agree to the use of a PBGC-approved procedure in a particular case.

For a further discussion of arbitration procedures in multiemployer pension plans, as well as substantive issues addressed in arbitration proceedings, see Withdrawal Liability Assessments by Multiemployer Defined Benefit Pension Plans.

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Jordan is an experienced litigator who specializes in complex commercial litigation and disputes. Jordan's primary practice focuses on the prosecution and defense of ERISA litigation matters including representation of plan sponsors, plan fiduciaries, financial advisors, plan participants, company executives, third-party administrators, employers, and others in a broad range of ERISA disputes, including breach of fiduciary duty, denial of benefit, Employee Stock Ownership Plan and deferred compensation matters. Jordan's multifaceted litigation practice also includes expertise in restructuring and insolvency matters, securities class actions, insurance fraud prosecution, and false claims act litigation. Jordan has been recognized for his legal work and has been named a Rising Star by Super Lawyers Magazine for the New York Metro area. Jordan is a regular columnist for Thomson Reuters' Journal of Compensation and Benefits, is a contributing author of the latest edition of Norton Bankruptcy Law and Practice; has written for publications including Bloomberg Law, Lexis Nexis Practice Advisor and Morningstar Advisor; and has been quoted in publications such as Law 360, Pensions & Investments and FundFire.

Jordan received his Juris Doctor from New York Law School, a Bachelor of Science from Vanderbilt University and compleed a Postdoctoral Fellowship in Corporate Governance and Business Ethics at Yale University. He is admitted to practice law in New York, New Jersey, Illinois and Massachusetts.

Barry L. Salkin, Counsel, The Wagner Law Group

Barry Salkin concentrates his practice in ERISA and employee benefits law. He has significant expertise drafting, amending and negotiating various ERISA and employee benefit plans, including defined benefit pension plans, profit sharing plans, 401(k) plans, as well as qualified and non-qualified deferred compensation programs. He also has wide-ranging experience crafting group medical and health plans involving Health Care Reform, HIPAA, and COBRA. In addition, he has represented clients in ERISA litigation and audits.

His clients include multi-national corporations, closely-held companies, high-net-worth individuals, financial institutions, governmental agencies, investment groups, and tax-exempt organizations such as hospitals and physicians' organizations.

Barry also advises clients on all aspects of retirement plan tax-qualification requirements and the application of labor and securities laws and regulations to sponsors of employee benefit plans and executive compensation programs. Moreover, he has extensive experience in establishing, merging and terminating benefit plans and compensation agreements, and counsels clients on fiduciary responsibilities and prohibited transactions.

Prior to joining The Wagner Law Group, Barry served as counsel and senior attorney at leading law firms in Manhattan.

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