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ERISA attorneys fear 'chilling effect' of American Airlines 401(k) ESG ruling

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Defined contribution plans using environmental, social and governance principles have suffered a setback and could face more litigation risk, following a Texas federal judge's [Jan. 10 ruling](#) against American Airlines and its 401(k) plan fiduciaries, some ERISA attorneys warn.

"I think this decision will have a chilling effect on ESG investment by employee benefit plans because it found liability despite evidence that American engaged in a prudent process," said Carol I. Buckmann, founding partner of law firm Cohen & Buckmann.

"Even if this decision is reversed, the fact that a court had gone to actual judgment for ERISA violations in the ESG context may well have a chilling effect on the taking into account of ESG considerations by ERISA fiduciaries, in the near term and maybe into the foreseeable future," said Andrew L. Oringer, partner and general counsel at The Wagner Law Group.

"ERISA fiduciaries tend to be conservative, and this kind of additional risk may well turn even pro-ESG fiduciaries in a 'who needs this' direction," he said.

U.S. District Court Judge Reed O'Connor ruled Jan. 10 that American and fiduciaries of two retirement plans had violated ERISA because they placed the interests of the company in plan management and investment decision-making.

"The court concludes that the facts compellingly demonstrated that defendants breached their fiduciary duty by failing to loyally act solely in the retirement plan's best financial interests by allowing their corporate interests, as well as [BlackRock's](#) ESG interests, to influence management of the plan," O'Connor wrote in his Jan. 10 opinion.

"The facts do not compel the same result for the duty of prudence," the judge wrote. "Defendants acted according to prevailing industry practices, even if leaders in the fiduciary industry contrived to set the standard."

ERISA has two broad categories of guidelines for employers: the duty of prudence, which governs the proper processes in plan management, and the duty of loyalty, which focuses on actions that place participants' interests above those of employers.

ERISA attorneys say plaintiffs usually must demonstrate a fiduciary breach for prudence before securing a ruling on duty of loyalty. However, O'Connor ruled against American Airlines and its fiduciaries for violating duty of loyalty while saying they acted prudently.

“Some courts have found that breaches of the duty of loyalty and the duty of prudence are related, with the duty of loyalty claim following from a determination of a breach of the duty of prudence,” Buckmann said.

The judge “is straining to find a basis for liability due to an underlying concern that these investments as a class are inappropriate,” she added. “This is contrary to the basic investment rules in ERISA, which do not establish lists of permissible and impermissible types of investments.”

By focusing on the plaintiff's duty-of-loyalty strategy, “it would not be surprising to see later plaintiffs in other cases go to school on this approach,” Oringer added.

The judge citing an ERISA loyalty violation but not a prudence violation was “unusual,” wrote Nevin Adams, an attorney and former chief content officer for the American Retirement Association, in an analysis published by the National Association of Plan Advisors.

“The implications here are that a fiduciary could do what fiduciaries broadly are expected to do in terms of process, and still ignore their obligations to participants,” Adams wrote. “To some — including this writer — that may seem a distinction without a real difference.”

A former American Airlines pilot sued the company and plan fiduciaries for two 401(k) plans in June 2023 saying the plans' business with certain investment managers — including BlackRock — violated ERISA due to their investments, proxy voting and other actions that included support of ESG principles.

The complaint survived two motions to dismiss, and it was the subject of a four-day bench trial.

American Airlines representatives did not respond to requests for comment.

BlackRock isn't a defendant.

“We always act independently and with a singular focus on what is in the best financial interests of our clients,” a BlackRock spokeswoman wrote in an email. “Our only agenda is maximizing returns for our clients, consistent with their choices.”

The case is far from over.

“I would expect American to appeal, but based on its history, the Court of Appeals for the Fifth Circuit will probably not be sympathetic,” Buckmann said. The New Orleans-based court is perhaps the most conservative of federal appeals courts.

“If left to stand, the District Court opinion ... poses a serious threat to investors' right to rely on financial advisers and asset managers or make their own informed decisions about how to invest their retirement savings,” said Danielle Fugere, president and chief counsel of shareholder advocacy group As You Sow, in a Jan. 10 news release.

There's also more paperwork for the District Court. The judge ordered the parties to file by Jan. 31 claims of losses and who must prove or disprove the losses. O'Connor also told the parties to “identify what, if any, direct evidence links ESG investing to financial underperformance of the plans in a way that harmed” the participants.

American Airlines Inc. 401(k) Plan for Pilots had \$10.3 billion in assets, and the [American Airlines Inc.](#) 401(k) Plan had \$14.7 billion in assets as of Dec. 31, 2022. Both plans are based in Fort Worth, Texas, and the data for both is from the latest Form 5500.

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