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Is the Merger of Participant-Directed 401(K) Plans Subject to ERISA's Fiduciary Standards: An Analysis of the Franklin v. First Union Litigation and Its Aftermath

Bryan L. Tyson

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IS THE MERGER OF PARTICIPANT-DIRECTED 401(K) PLANS SUBJECT TO ERISA'S FIDUCIARY STANDARDS?: AN ANALYSIS OF THE *FRANKLIN V. FIRST UNION* LITIGATION AND ITS AFTERMATH

Bryan L. Tyson*

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* Mr. Tyson received a J.D. with Honors from UNC-Chapel Hill in 1996 and an LL.M. in Taxation with Distinction from Georgetown University Law Center in 2002. Mr. Tyson is a member of the Georgia and Texas State Bars. The views expressed herein are solely those of the author.

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I. INTRODUCTION

Employer-sponsored pension plans, especially those in which participants may direct their investments, are common in the American workplace.¹ Equally common is the likelihood that the employer sponsoring such a plan will be a party to a reorganization in which it, along with its 401(k) plan,² will merge with another company.³ When a merger of 401(k) plans occurs, the roles of the

¹ As of 1997, 401(k) plans "accounted for 37 percent of qualified private retirement plans, 48 percent of active employees, and 65 percent of new contributions." JACK L. VANDERHEI, EBRI SPECIAL REPORT: COMPANY STOCK IN 401(K) PLANS: RESULTS OF A SURVEY OF ISCEBS MEMBERS 2 (January 28, 2002) (citing United States Dept. of Labor, Pension and Welfare Benefits Administration, "Abstract of 1997 Form 5500 Annual Reports," Private Pension Plan Bulletin No. 10, Winter 2001, Washington, D.C.). Similarly, they were the only employer-sponsored plan available for approximately half of their 33 million active participants. U.S. Dept. of Labor, Pension and Welfare Benefits Administration, Private Pension Plan Bulletin, Abstract of 1997 Form 5500 Annual Reports Table D5 (1997). According to the Profit Sharing/401(k) Council of America, as of the year 2000, 401(k) plans will have 43,200,000 participants and 1.7 trillion dollars in assets. Profit Sharing/401(k) Council of America, *Growth of 401(k) Eligible Participants, Assets and Plans 1984-2000*, at <http://www.pasca.org/data/dcstats2.asp> (last visited April 21, 2002).

Although not all 401(k) plans are participant-directed, most are: according to a recent survey by the Profit Sharing/401(k) Council of America, 97 percent of companies surveyed allowed participants to direct their own contributions, while 84.4 percent allowed them to direct company contributions. Profit Sharing/401(k) Council of America, *Defined Contribution Plans 1978-2000*, at <http://www.pasca.org/data/dcstats5.asp> (last visited April 21, 2002).

² See *infra* note 12 and accompanying text (discussing definition and features of a 401(k) plan).

³ The Federal Trade Commission ("FTC") has described the United States as being "in the

employer as a plan sponsor⁴ and fiduciary appear, at first glance, to collide. Normally, a plan sponsor may adopt, terminate, or modify a plan without implicating fiduciary responsibilities under the Employee Retirement Income Security Act (“ERISA” or “the Act”)⁵ because these are “settlor” functions that do not implicate ERISA’s fiduciary duties.⁶ When merging two or more plans, however, a plan sponsor will likely cancel the acquired corporation’s investment alternatives in its 401(k) plan. When plan sponsors select investment alterna-

midst of a ‘merger wave.’” Federal Trade Commission, *Promoting Competition, Protecting Consumers: A Plain English Guide to Antitrust Laws*, at <http://www.ftc.gov/bc/compguide/mergers.htm> (last visited Apr. 26, 2002). “Over the past decade, the number of mergers reported to the FTC and the Justice Department has more than tripled, increasing from 1,529 transactions in fiscal year 1991 to 4,642 in fiscal year 1999.” SIMON M. LORNE & JOY MARLENE BRYAN, 11A ACQUISITIONS AND MERGERS: NEGOTIATED AND CONTESTED TRANSACTIONS § 7.2 (Supp. 2002).

⁴ A plan sponsor is the person or entity that establishes that plan for its employees. ERISA § 3(16)(B), 29 U.S.C. § 1002 (16)(B) (2001) (defining “plan sponsor”). In the case of a single employer who establishes or maintains an employee benefit plan, the plan sponsor is defined as the employer. *Id.* The employer, however, is also given the status of “plan administrator” if none is designated by the terms of the instrument under which the plan is operated. *Id.* § 3(16)(A)(ii), 29 U.S.C. § 1002(16)(A)(ii).

⁵ ERISA, codified at 29 U.S.C. §§ 1000-1461, is the federal law governing most employer-sponsored pension plans. It applies to “employee pension benefit plans,” which are defined as

any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program—

- (i) provides retirement income to employees, or
- (ii) results in a deferral of income by employees for periods extending to the termination of covered employment or beyond,

regardless of the method of calculating the contributions made to the plan, the method of calculating the benefits under the plan or the method of distributing benefits from the plan.

Id. § 3(2)(A), 29 U.S.C. § 1002(2)(A).

⁶ *See, e.g.,* Hughes Aircraft Co. v. Jacobson, 525 U.S. 432, 444 (1999) (“In general, an employer’s decision to amend a pension plan concerns the composition or design of the plan itself and does not implicate the employer’s fiduciary duties which consist of such actions as the administration of the plan’s assets.”); Lockheed Corp. v. Spink, 517 U.S. 882, 890 (1996) (“Plan sponsors who alter the terms of a plan do not fall into the category of fiduciaries.”); Curtiss-Wright Corp. v. Schoonejongen, 514 U.S. 73, 78 (1995) (“ERISA does not create any substantive entitlement to employer-provided health benefits or any other kind of welfare benefits. Employers or other plan sponsors are generally free under ERISA, for any reason at any time, to adopt, modify, or terminate welfare plans.”); Letter from Dennis M. Kass, Assistant Secretary, Department of Labor, to John N. Erlenborn (Mar. 13, 1986) (on file with author) (“In light of the voluntary nature of the private pension system governed by ERISA, the Department [of Labor] has concluded that there is a class of discretionary activities which relate to the formation, rather than the management, of plans. These so-called ‘settlor’ functions include decisions relating to the establishment, termination and design of plans and are not fiduciary activities subject to Title I of ERISA.”).

tives for their participant-directed 401(k) plans, they act as fiduciaries and are subject to the panoply of fiduciary obligations imposed by ERISA.⁷ Does the plan sponsor become a fiduciary by canceling these investment alternatives because it thereby selected (or, more appropriately, de-selected) investment alternatives for its 401(k) plan? Or does the plan sponsor remain a non-fiduciary because it is simply amending or modifying a plan by merging its plan with the acquired corporation's plan?

No case has definitively addressed the tension between these two black-letter ERISA principles. Recently, however, in *Franklin v. First Union Corp.*,⁸ former participants in Signet Bank's 401(k) plan sued First Union after Signet and its 401(k) plan were merged into First Union and the investment alternatives in the Signet plan were cancelled.⁹ The plaintiffs alleged that by treating the Signet 401(k) plan investments in this manner, First Union selected investment alternatives for the former Signet employees and thereby acted in a fiduciary capacity.¹⁰

This paper argues that courts construing a plan sponsor's duties in merging participant-directed 401(k) plans should hold that no fiduciary duty exists to examine the investment alternatives in the acquired company's 401(k) plan. Part II of the paper summarizes ERISA's fiduciary duty requirements, the requirements for retirement plans to qualify for the preferential tax treatment provided by Internal Revenue Code ("IRC") § 401(k), and the requirements for allowing participants to direct the investment of their assets under ERISA § 404(c). Part III examines the *Franklin v. First Union Corp.*¹¹ litigation, specifically the allegations related to fiduciary duties of plan sponsors in the merger of participant-directed 401(k) plans. Part IV analyzes the theories of fiduciary responsibility advocated by the employee plaintiffs in *First Union* using courts' usual methods of interpreting ERISA. Finally, based on the methods most commonly used to interpret ERISA, Part V concludes that plan sponsors should not be held to fiduciary standards when they cancel investment alternatives in the participant-directed 401(k) plan of their merger partners.

⁷ See, e.g., 57 Fed. Reg. 46906, 46924 n.27 (1992) ("In this regard, the Department points out that the act of limiting or designating investment options that are intended to constitute all or part of the investment universe of an ERISA 404(c) plan is a fiduciary function."); Department of Labor, Pension & Welfare Benefit Programs Opinion 97-15A (May 22, 1997) (finding that bank exercised "discretionary authority and control," and was thereby a "fiduciary" under ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A) (2001), because the bank reserved the right to add or delete mutual funds in which it allowed pension plans to invest). Cf. 29 C.F.R. § 2550.404c-1(a)(2) (2002) (stating that standards in 404(c) regulation only apply to determine whether a plan is an ERISA 404(c) plan and do not affect other fiduciary duties under ERISA).

⁸ 84 F. Supp. 2d 720 (E.D. Va. 2000).

⁹ See *infra* Part III (discussing merger between First Union and Signet Bank, including merger of participant-directed 401(k) plans of the companies).

¹⁰ See *infra* note 88 and accompanying text.

¹¹ 84 F. Supp. 2d 720 (E.D. Va. 2000).

II. ERISA'S FIDUCIARY DUTIES, PARTICIPANT-DIRECTED 401(K) PLANS, AND REQUIREMENTS UPON PLAN MERGER

Under ERISA, the fiduciary duties associated with selecting investment alternatives for participant-directed 401(k) plans are different than the general duties imposed on plan sponsors in the merger of pension plans. Therefore, it is important to review each before examining whether the two overlap. This section provides several preliminary definitions necessary to understand 401(k) plans and the scope of fiduciary duties. The section then outlines the various legal principles underpinning the concepts of fiduciary duties associated with investment alternative selection and ERISA's specific requirements for merging pension plans.

A. Preliminary Definitions

1. "401(k) Plans"

A "401(k)" plan is based on a "cash or deferred arrangement" or "CODA."¹² Under this arrangement, participants contribute a portion of their salary to a qualified retirement plan¹³ instead of having the cash paid directly to them.¹⁴ The amounts deferred by participants to the 401(k) plan are made on a pre-tax basis (as opposed to having the amounts distributed directly to the participants as wages, where they would be subject to immediate income taxation).¹⁵ Amounts so deferred by participants are called "elective contributions."¹⁶ Elective contributions are to be distinguished from both employer matching contributions, which are contributions employers make to the 401(k)

¹² Such plans are called "401(k) plans" because § 401(k) of the IRC authorizes this cash or deferred arrangement.

¹³ A "qualified retirement plan" is "one that satisfies the requirements, in both form and operation, of the applicable provisions of the Internal Revenue Code." PAMELA PERDUE, QUALIFIED PENSION AND PROFIT-SHARING PLANS ¶ 1.01 (2d ed. 2001-2002). Such qualification requirements are generally listed in § 401(a) of the IRC.

¹⁴ I.R.C. § 401(k) (2001).

¹⁵ Thomas S. Gigot, *401(k) Plan Litigation under ERISA*, 27 J. PENSION PLAN & COMPLIANCE 63 (Oct. 1, 2001).

¹⁶ Although elective contributions defer money that would otherwise be paid to the participant as salary, the IRS considers them to be employer money. See PERDUE *supra* note 13, ¶ 17.05[3]. The Department of Labor, however, considers elective contributions to be the property of the participant. Regulation Relating to Definition of "Plan Assets"—Participant Contributions, 61 Fed. Reg. 41220 n.1 (August 7, 1996) (codified at 29 C.F.R. § 2510.3-102) ("The Department's view is that elective contributions to an employee benefit plan, whether made pursuant to a salary reduction agreement or otherwise, constitute amounts paid to or withheld by an employer (i.e., participant contributions) within the scope of § 2510.3-102, without regard to the treatment of such contributions under the Internal Revenue Code.").

plan that are not elective contributions, and after-tax employee contributions, which some 401(k) plans allow.¹⁷

The types of qualified retirement plans that may provide for a 401(k) feature include a profit-sharing plan,¹⁸ a stock bonus plan,¹⁹ a pre-ERISA money purchase plan,²⁰ or a rural cooperative plan.²¹ All of these types of plans, and hence any 401(k) plan, are “defined contribution plans.” A defined contribution plan “means a pension plan which provides for an individual account for each participant and for benefits based solely on the amount contributed to the participant’s account, and any income, expenses, gains and losses, and any forfeitures of accounts of other participants which may be allocated to such participant’s account.”²² In a defined contribution plan, the ultimate benefit that will result from such investments is not guaranteed.²³

2. Fiduciary

a. *The Functional and Transactional Nature of the Definition of Fiduciary*

Under ERISA, a person²⁴ is a fiduciary

to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any mon-

¹⁷ PERDUE, *supra* note 13, ¶ 17.05[3].

¹⁸ *Id.* at ¶ 1.05[1] (defining profit-sharing plan).

¹⁹ *Id.* at ¶ 1.05[9] (defining stock bonus plan).

²⁰ A pre-ERISA money purchase pension plan is a defined contribution plan that: (1) was in existence on June 27, 1974, (2) included a qualified salary reduction agreement, and (3) provides for employer and participant contributions of amounts not in excess of that specified by the contribution formula in the plan. I.R.C. § 401(k)(6) (2001).

²¹ A rural cooperative plan is a defined contribution plan established and maintained by a rural cooperative. *Id.* § 401(k)(7); *see also id.* § 401(k)(7)(B) (defining “rural cooperative”).

²² ERISA § 3(34), 29 U.S.C. § 1002(34) (2001). The IRC defines a “defined contribution plan” in almost the exact same language. I.R.C. § 414(i) (2001) (defining “defined contribution plan”).

²³ *Nachman Corp. v. Pension Benefit Guaranty Corp.*, 446 U.S. 359, 364 n.5 (1980) (“[U]nder such [defined contribution] plans, by definition, there can never be an insufficiency of funds in the plan to cover promised benefits.”).

²⁴ ERISA defines a person as “an individual, partnership, joint venture, corporation, mutual company, joint-stock company, trust, estate, unincorporated organization, association, or employee organization.” ERISA § 3(9), 29 U.S.C. § 1002(9).

neys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan.²⁵

This definition of “fiduciary,” therefore, is “functional” because a person will be a fiduciary (and hence subject to fiduciary duties under ERISA)²⁶ based on the actions he performs. “[T]he definition includes persons who have authority and responsibility with respect to the matter in question, regardless of their formal title.”²⁷ Some persons are considered fiduciaries because of the position or title they hold, but only because their title or position requires them to perform one of the above-listed actions. For example, as noted by the Department of Labor, an administrator of an employee benefit plan must, by the very nature of his position, have “discretionary authority or discretionary responsibility in the administration of the plan,” and therefore is a fiduciary by reason of this authority or responsibility.²⁸ Other positions, however, must be examined to determine whether a person is performing one or more of the above-listed duties to determine whether he is a fiduciary and therefore subject to ERISA’s fiduciary requirements.²⁹

The definition of fiduciary under ERISA is also transactional. A person is a fiduciary only with respect to specific transactions in which he acts in a fiduciary capacity. An individual who acts in a fiduciary capacity for some matters with respect to an employer may not be a fiduciary regarding other plan matters for the same employer. The role of a member of a board of directors illustrates this principle:

Members of the board of directors . . . will be fiduciaries only to the extent that they have responsibility for the functions described in section 3(21)(A) of the Act. For example, the board of directors may be responsible for the selection and retention of plan fiduciaries. In such a case, members of the board of directors exercise “discretionary authority or discretionary control respecting management of such plan” and are, therefore, fiduciaries with respect to the plan. *However, their responsibility,*

²⁵ *Id.* § 3(21)(A), 29 U.S.C. § 1002(21)(A).

²⁶ *See, e.g., id.* § 404, 29 U.S.C. § 1104 (2001) (describing the general duties of fiduciaries).

²⁷ H.R. CONF. REP. NO. 93-1280 (1974), *reprinted in* 1974 U.S.C.C.A.N. 4639, 5038, 5103.

²⁸ 29 C.F.R. § 2509.75-8, D-3 (2002).

²⁹ *Id.*

*and, consequently, their liability, is limited to the selection and retention of fiduciaries.*³⁰

Based on this interpretation of the definition of fiduciary, a person is a fiduciary only when performing the functions listed in § 3(21)(A) of the statute, and only with respect to the transactions in which he performs those functions.

b. Named Fiduciary

As stated above, some persons are ERISA fiduciaries because they are named as such. A “named fiduciary” is

a fiduciary who is named in the plan instrument, or who, pursuant to a procedure specified in the plan, is identified as a fiduciary (A) by a person who is an employer or employee organization with respect to the plan or (B) by such an employer and such an employee organization acting jointly.³¹

Under ERISA, every employee benefit plan must be “established and maintained pursuant to a written instrument. Such instrument shall provide for one or more named fiduciaries who jointly or severally shall have authority to control and manage the operation and administration of the plan.”³²

3. Trustee

ERISA provides that one or more trustees must hold all assets of pension plans in trust.³³ Although the trustee can be either named in the trust document or appointed by the named fiduciary, the trustee must affirmatively accept his position.³⁴ Upon acceptance, the trustee is charged with the “exclusive authority to manage and control the assets of the plan.”³⁵ Generally, the only exceptions to this grant of exclusive responsibility occur when (1) the pension plan expressly provides that the trustee is subject to the direction of the named fiduciary and the named fiduciary provides the trustee with proper direc-

³⁰ *Id.* at D-4 (emphasis added); see also *Chicago Bd. of Options v. Connecticut Gen. Life Ins. Co.*, 713 F.2d 254, 259 (7th Cir. 1982) (“It is important to remember that if Connecticut General is a fiduciary because of the power to amend, this status only governs actions taken in regard to amending the contract and does not impose fiduciary obligations upon Connecticut General when taking other actions.”) (citations omitted).

³¹ ERISA § 402(a)(2), 29 U.S.C. § 1102(a)(2) (2001).

³² *Id.* § 402(a)(1), 29 U.S.C. § 1102(a)(1).

³³ *Id.* § 403(a), 29 U.S.C. § 1103(a) (2001).

³⁴ *Id.*

³⁵ *Id.*

tions made in accordance with the plan documents and which are not contrary to the requirement of ERISA, or (2) “authority to manage, acquire, or dispose of assets of the plan is delegated to one or more investment managers.”³⁶ Because of his exclusive authority to manage and control the assets of the plan, the trustee will be a fiduciary who is subject to the fiduciary standards of ERISA when dealing with the plan as a trustee.³⁷

4. Participant-Directed 401(k) Plans

Although the trustee, who is a fiduciary, has exclusive authority to manage and control the assets of a pension plan, ERISA § 404(c) relieves fiduciaries of liability for plan investments if certain “safe harbor” conditions are met.³⁸ Specifically, these conditions require: (1) that the participant or beneficiary be given an opportunity to exercise control over the assets in his individual account, and (2) that the plan provides the participant or beneficiary the opportunity to choose the manner in which his plan assets are allocated, where such choice is allowed among a broad range of investment alternatives.³⁹ Plans satisfying these conditions are often termed “participant-directed 401(k) plans.”⁴⁰

With respect to the “broad range” of investment alternatives available to participants, there are generally three requirements that must be met for a plan to qualify as an ERISA § 404(c) plan. First, the participant must be given an opportunity to affect materially the return on his account balance and the degree of risk to which the account is subject.⁴¹ Second, the participant must be provided an opportunity to choose from at least three diversified investment alternatives, each with materially different risk and reward characteristics.⁴² Third, the par-

³⁶ *Id.*; see *supra* Part II.A.2.b (discussing definition and responsibilities of a “named fiduciary”). An “investment manager” is a fiduciary with responsibility for the management and disposition of plan assets. The investment manager must be a registered investment manager under the Investment Advisors Act of 1940, a bank, or an insurance company qualified to manage or dispose of employee pension plan assets; the investment manager must acknowledge his status as a fiduciary in writing. ERISA § 3(38); 29 U.S.C. § 1002(38) (2001).

³⁷ ERISA defines a fiduciary as any person who “exercises any authority or control respecting management or disposition of [pension plan] assets.” ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A).

³⁸ *Id.* § 404(c), 29 U.S.C. § 1104(c) (2001).

³⁹ *Id.* § 404(c)(1), 29 U.S.C. § 1104(c)(1); 29 C.F.R. § 2550.404c-1 (2002).

⁴⁰ Such plans are also called “ERISA section 404(c) plans” because § 404(c) and its accompanying regulations describe the general requirements for these plans.

⁴¹ 29 C.F.R. § 2550.404c-1(b)(3).

⁴² *Id.* In the aggregate, these investment alternatives must permit the participant to achieve risk and reward characteristics normally appropriate for the participant. *Id.* The individual investment alternatives must also, when combined with the other alternatives in the plan, minimize overall risk of the portfolio through diversification. *Id.*

participant must be given an opportunity to diversify his investments to minimize the risk of large losses.⁴³

B. *Fiduciary Duties*

1. General Fiduciary Duties with Respect to Investment of Assets

As discussed above, the responsibility for investing assets of the plan on behalf of participants and beneficiaries rests with the trustee of the plan, who is a fiduciary.⁴⁴ When a fiduciary invests plan assets, ERISA requires him to discharge his duties solely in the interest of and for the exclusive benefit of participants and beneficiaries; he must also act with the care and skill of a prudent man in similar circumstances. The fiduciary must also diversify the investments of the plan to minimize the risk of large losses and discharge his duties in accordance with the terms of the documents governing the plan.⁴⁵ Failure to fulfill such duties can result in a breach of fiduciary duty and liability for damages to the plan.⁴⁶

⁴³ *Id.*

⁴⁴ See *supra* note 35 and accompanying text.

⁴⁵ ERISA § 404(a)(1) provides:

[A] fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—

- (A) for the exclusive purpose of
 - (i) providing benefits to participants and their beneficiaries; and
 - (ii) defraying reasonable expenses of administering the plan;
- (B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims;
- (C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and
- (D) in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of this subchapter [subchapter I] and subchapter III of this chapter.”).

ERISA § 404(a)(1), 29 U.S.C. § 1104(a)(1) (2001).

Subchapter I of ERISA, codified at 29 U.S.C. §§ 1001-1191c (2001), provides rules for the protection of employee benefit rights, while subchapter III establishes the Pension Benefit Guaranty Corporation and a plan termination insurance program.

⁴⁶ *Id.* § 409(a), 29 U.S.C. § 1109(a) (2001); *id.* § 502(a), 29 U.S.C. § 1132 (2001).

2. Relief from Fiduciary Liability for Losses Resulting from the Participant's Exercise of Control

In a participant-directed ERISA § 404(c) plan, however, the fiduciary is not liable for losses that result from the participant's exercise of control over the assets in the participant's account; moreover, the participant—despite his discretion over the investment of plan assets—is not considered a fiduciary.⁴⁷ The fiduciary is nonetheless liable both for the investment alternatives offered to a participant, as well as for periodic review of such investments to determine whether to retain them as investment alternatives.⁴⁸

This limited relief from liability for the fiduciary originates from the Department of Labor's interpretation of the following statutory language: "[N]o person who is otherwise a fiduciary shall be liable . . . for any loss . . . which results from [a] participant's or beneficiary's exercise of control."⁴⁹ This relief from liability extends only to losses that are "the direct and necessary result of that participant's or beneficiary's exercise of control."⁵⁰ For example, if the fiduciary does not offer the participant a broad range of investment alternatives, then the 404(c) relief from liability is inapplicable and any resulting losses are not based on the participant's exercise of control of the plan. Rather, the losses result from the fiduciary's failure to offer an appropriately broad selection of investment alternatives to minimize the risk of loss. "In other words, a plan fiduciary can never avoid potential liability for negligence in picking the investments which constitute the 'menu' of investment alternatives made available to participants under the plan or any investment advisor connected with such investment alternatives."⁵¹

C. General Plan Sponsor Duties

While ERISA and its accompanying regulations set forth the duties of fiduciaries in all aspects of fiduciary activity in great detail,⁵² neither the statute nor the regulations place responsibility on plan sponsors.⁵³ A plan sponsor's lack of responsibility emanates from the voluntary nature of the private pension

⁴⁷ *Id.* § 404(c)(1)(A), (B), 29 U.S.C. § 1104(c)(1)(A), (B); 29 C.F.R. § 2550.404c-1(d)(1), (2) (2002). Without this specific declaration that the participant in control of the assets of his account is not a fiduciary, any other fiduciary under the plan could be liable as a "co-fiduciary" for the participant's losses or other breach of fiduciary duties. ERISA § 405, 29 U.S.C. § 1105 (2001).

⁴⁸ See *supra* note 7 and accompanying text.

⁴⁹ ERISA § 404(c)(1)(B), 29 U.S.C. § 1104(c)(1)(B).

⁵⁰ 29 C.F.R. § 2550.404c-1(d)(2).

⁵¹ Morton A. Harris, *Working with Participant Directed Investments Under ERISA § 404(c)*, SG008 A.L.I.-A.B.A. 887, 908-09 (2001).

⁵² See, e.g., ERISA § 404, 29 U.S.C. § 1104.

⁵³ See *supra* note 4 (defining "plan sponsor" under ERISA and describing duties).

system in the United States;⁵⁴ ERISA does not require an employer to establish a pension plan.⁵⁵ Plan sponsors are therefore free to establish, modify, or terminate a plan at any time.⁵⁶

Plan sponsors, however, can “wear two hats” under ERISA by serving as both a plan sponsor and a fiduciary.⁵⁷ If a plan sponsor performs a fiduciary act, that plan sponsor is a fiduciary to the extent of the fiduciary act performed.⁵⁸ When acting in a fiduciary capacity, the plan sponsor must comply with ERISA’s fiduciary standards, including those applicable to selection of investment alternatives for a participant-directed 401(k) plan.⁵⁹

D. ERISA Requirements on Merger of Retirement Plans

Both ERISA and the IRC specify how plans covered under their respective provisions⁶⁰ must be merged.⁶¹ ERISA § 208 provides:

⁵⁴ *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 91 (1983) (“ERISA does not mandate that employers provide any particular benefits”); *see also* *Curtiss-Wright Corp. v. Schoonejongen*, 514 U.S. 73, 78 (1995) (“ERISA does not create any substantive entitlement to employer-provided health benefits or any other kind of welfare benefits. Employers or other plan sponsors are generally free under ERISA, for any reason at any time, to adopt, modify, or terminate welfare plans.”).

⁵⁵ Letter from Dennis M. Kass, Assistant Secretary, Department of Labor, to John N. Erlenborn (Mar. 13, 1986) (on file with author) (“In light of the voluntary nature of the private pension system governed by ERISA, the Department [of Labor] has concluded that there is a class of discretionary activities which relate to the formation, rather than the management, of plans. These so-called ‘settlor’ functions include decisions relating to the establishment, termination and design of plans and are not fiduciary activities subject to Title I of ERISA.”).

⁵⁶ *See supra* note 6 and accompanying text.

⁵⁷ *Belade v. ITT Corp.*, 909 F.2d 736, 738 (2d Cir. 1990) (per curiam) (“ERISA permits employers to wear ‘two hats,’ and [employers] assume fiduciary status ‘only when and to the extent that they function in their capacity as plan administrators, not when they conduct business that is not regulated by ERISA.’”) (quoting *Amato v. Western Union Int’l*, 773 F.2d 1402, 1416-17 (2d Cir. 1985)).

⁵⁸ *See supra* Part II.A.2.a. (discussing functional and transactional nature of fiduciary definition).

⁵⁹ 29 C.F.R. § 2509.75-8, D-4 (2002) (“Members of the board of directors of an employer which maintains an employee benefit plan will be fiduciaries only to the extent that they have responsibility for the functions described in section 3(21)(A) of the Act [defining “fiduciary”].”).

⁶⁰ ERISA generally applies to “employee welfare benefit plans” and “employee pension benefit plans,” as those terms are defined in the Act. ERISA § 4, 29 U.S.C. § 1003 (2001) (defining coverage of ERISA); *see also id.* § 3(1), (2), 29 U.S.C. § 1002(1), (2) (2001) (defining employee welfare benefit plan and employee pension benefit plan); *supra* note 5 (defining “employee pension benefit plan”); *infra* note 115 (defining “employee welfare benefit plan”). Unlike ERISA, the IRC does not apply to specific types of employee benefit plans; rather, it establishes the requirements for plans to be considered “qualified,” meaning that they are eligible for favorable tax treatment to the plan sponsor, the plan participants, and the trust containing plan assets. I.R.C. § 401(a) (2001) (listing qualification requirements for qualified plans); *id.* § 402(a) (2001) (providing exemption from taxation for plan participants with respect to contributions to plan); *id.* § 404(a) (2001) (providing deduction to plan sponsor for contributions to qualified plan); *id.* §

A pension plan may not merge or consolidate with, or transfer its assets or liabilities to, any other plan . . . unless each participant in the plan would (if the plan then terminated) receive a benefit immediately after the merger, consolidation, or transfer which is equal to or greater than the benefit he would have been entitled to receive immediately before the merger, consolidation, or transfer (if the plan had then terminated).⁶²

Likewise, § 414(l) of the IRC provides that a plan is not “qualified”⁶³ unless

in the case of any merger or consolidation of the plan with, or in the case of any transfer of assets or liabilities of such plan to, any other trust plan . . . each participant in the plan would (if the plan then terminated) receive a benefit immediately after the merger, consolidation, or transfer which is equal to or greater than the benefit he would have been entitled to receive immediately before the merger, consolidation, or transfer (if the plan had then terminated).⁶⁴

The Treasury regulations interpreting ERISA⁶⁵ § 208 and IRC § 414(l) explicitly provide the requirements for merger of defined contribution plans, including 401(k) plans:

In the case of a merger of two or more defined contribution plans, the requirements of section 414(l) will be satisfied if all of the following conditions are met:

- (1) The sum of the account balances in each plan equals the fair market value (determined as of the date of the merger) of the entire plan assets.

501(a) (2001) (providing exemption from taxation for trust holding qualified plan assets); *see also supra* note 13 (defining “qualified retirement plan”).

⁶¹ A “merger” of pension plans means “the combining of two or more plans into a single plan.” Treas. Reg. § 1.414(l)-1(b)(2) (2002).

⁶² ERISA § 208, 29 U.S.C. § 1058 (2001).

⁶³ *See supra* note 13 (defining “qualified retirement plan”).

⁶⁴ I.R.C. § 414(l)(1) (2001).

⁶⁵ “In the ERISA Reorganization Plan of 1978 the Treasury Department was assigned responsibility for issuing regulations under certain provisions of ERISA, including § 1058. Thus, ‘all regulations implementing the provisions of [§§ 1058 and 414(l)] have been promulgated by the Secretary of the Treasury, mostly under § 414(l) of the Internal Revenue Code.’” *Malia v. General Elec. Co.*, 23 F.3d 828, 832 n.4 (3rd Cir. 1994) (quoting *Van Orman v. American Ins. Co.*, 608 F. Supp. 13, 25 n.3 (D.N.J. 1984)).

(2) The assets of each plan are combined to form the assets of the plan as merged.

(3) Immediately after the merger, each participant in the plan as merged has an account balance equal to the sum of the account balances the participant had in the plans immediately prior to merger.⁶⁶

III. FRANKLIN V. FIRST UNION CORP. LITIGATION

A. General Background of the Merger of Signet Bank and First Union

In *Franklin v. First Union Corp.*,⁶⁷ the concepts of (1) plan sponsors' lack of fiduciary duties when terminating or modifying a plan, and (2) the fiduciary nature of selection of investment alternatives, came crashing together. The *First Union* case arose after the 1997 merger of First Union Corporation, a North Carolina-based banking corporation, and Signet Bank, a Virginia-based banking corporation.⁶⁸

Prior to the merger, the employees of Signet Bank were participants in the Signet Banking Corporation Employee Savings Plan (the "Signet Plan"), a 401(k) plan.⁶⁹ The Signet Plan was administered by a committee (the "Signet Committee") comprised of members appointed by Signet's board of directors.⁷⁰ The Signet Plan provided that the Signet Committee was to select the various investment alternatives in which participants could invest. In selecting these alternatives, the Signet Committee was to comply with ERISA's § 404(c) regulations so that the plan would be participant-directed.⁷¹ The Committee initially selected seven investment alternatives for the Signet Plan: (1) the Signet Common Stock Fund,⁷² (2) the Vanguard Index 500 Trust Portfolio,⁷³ (3) the American Century/Twentieth Century Ultra Investors Fund,⁷⁴ (4) the Virtus Treasury Money Market Fund, (5) the Virtus Stable Value Fund, (6) the Virtus U.S. Government Securities Fund, and (7) the Virtus Style Manager.⁷⁵ At a later date, the

⁶⁶ Treas. Reg. § 1.414(l)-1(d) (2002).

⁶⁷ 84 F. Supp. 2d 720 (E.D. Va. 2000).

⁶⁸ *Id.* at 722-23.

⁶⁹ *Id.* at 721-22.

⁷⁰ *Id.* at 721.

⁷¹ *Id.* at 722.

⁷² *Id.* This was a stock fund that invested solely in Signet common stock. *Id.*

⁷³ This was a mutual fund that invested in the Standard and Poor's 500 Index. *Id.*

⁷⁴ This was also a mutual fund. *Id.*

⁷⁵ *Id.* The Virtus funds were proprietary mutual funds of Signet. *Id.*

Signet Committee added an eighth option, the Capital One Stock Fund.⁷⁶ This fund invested solely in the stock of Capital One Financial Corporation, a subsidiary of Signet Bank whose stock was “spun-off” to Signet Bank shareholders.⁷⁷

Like Signet, First Union maintained a 401(k) plan for its employees, known as the “First Union Plan.”⁷⁸ The First Union Plan offered participants seven investment alternatives into which they could invest their retirement funds; these alternatives were all proprietary funds operated by First Union.⁷⁹

B. *The Merger of the Signet and First Union 401(k) Plans*

As part of the merger of the two corporations, First Union transferred the assets of the Signet Plan to the First Union Plan.⁸⁰ To facilitate this transfer, there was a “black-out” period of approximately three weeks during which Signet Plan participants could not alter the investment alternatives into which their retirement funds were invested.⁸¹ Each participant’s former investment choices under the Signet Plan were “mapped” into four of the seven funds available under the First Union Plan.⁸² “When the ‘black-out’ period ended, former Signet

⁷⁶ *Id.*

⁷⁷ *Franklin v. First Union Corp.*, Memorandum in Support of Defendants’ Motion for Summary Judgment on Count IV, p. 5, at http://www.signetsuit.com/Defendant_Count_IV_Brief.doc (last visited April 28, 2002) (“[T]he Signet shares held by the Signet plan received a pro rata distribution of the shares of Cap[ital] One in the spin-off and were maintained under the Signet Plan in a separate fund. . . . In other words, the Signet Plan did not acquire the Cap[ital] One stock by an affirmative decision of its fiduciaries, but rather automatically as a shareholder of Signet Bank.”).

⁷⁸ *Franklin v. First Union Corp.*, 84 F. Supp. 2d 720, 721-22 (E.D. Va. 2000).

⁷⁹ *Id.* at 724; see also Cynthia A. Van Bogaert and Jeffrey J. Storch, *First Union and Plan Mergers*, 7 EMPLOYEE BENEFITS TAX J. 235, 236 (March/April 2000).

⁸⁰ *Franklin*, 84 F. Supp. 2d at 724.

⁸¹ *Id.* at 724-25. The black-out period lasted from December 23, 1997 until February 17, 1998. *Id.* at 725. The purpose of the black-out period was to “transfer the assets of the Signet Plan into the First Union Plan and get [the assets] ‘online’ with First Union’s telephonic administration system so the former Signet Plan participants could move their funds telephonically among investment options if they chose.” *Franklin v. First Union Corp.*, Memorandum in Support of Defendants’ Motion for Summary Judgment on Count IV, p. 5, at http://www.signetsuit.com/Defendant_Count_IV_Brief.doc (last visited April 28, 2002).

⁸² *Franklin*, 84 F. Supp. 2d at 724. “Mapping” refers to the process of selecting replacement funds in which to place assets formerly held in another fund that is no longer available as a result of the merger. Van Bogaert and Storch, *supra* note 79, at 236. The Capital One Stock Fund, the Virtus Stable Value Fund, and the Virtus Treasury Money Market Funds were mapped into the First Union Stable Fund; the Signet Company Stock Fund was mapped into the First Union Common Stock Fund; the Virtus U.S. Government Securities fund was mapped into the Evergreen U.S. Government Fund; and the Vanguard Index 500 Trust, the American Century Ultra Investors Fund and the Virtus Style Manager Fund were mapped into the First Union Enhanced Stock Market Fund. *Franklin v. First Union Corp.*, Memorandum in Support of Defendants’ Motion for

Plan participants were limited to the First Union-proprietary investment vehicles offered under the First Union Plan.”⁸³ Signet participants were, however, allowed to alter the investments in their accounts among these First Union proprietary funds.⁸⁴

C. *Claims of the Former Signet Employees*

As a result of the merger of the Signet Bank and First Union Plans and First Union’s cancellation of the investment alternatives available in the former Signet Plan, nine former employees of Signet Bank⁸⁵ filed a class-action lawsuit against First Union and various other defendants (“*Franklin I*”).⁸⁶ The complaint alleged, *inter alia*, that the Signet Plan participants had a vested right to the investment alternatives in the Signet Plan⁸⁷ and that “the First Union defendants breached their fiduciary duties in liquidating participants’ investments in the Signet Plan and in discontinuing its non-proprietary investment [alternatives].”⁸⁸ The plaintiffs’ allegations that First Union failed to examine any of the investment alternatives in the Signet Plan were further fueled by their allegations in a separate lawsuit, also against First Union.⁸⁹ The allegations in the

Summary Judgment on Count IV, p. 4, at http://www.signetsuit.com/Defendant_Count_IV_Brief.doc (last visited April 28, 2002); *see also* Van Bogaert and Storch, *supra* note 79, at 240 Ex.1 (showing mapping of Signet Plan investment alternatives into First Union Plan investment alternatives).

⁸³ *Franklin*, 84 F. Supp. 2d at 725.

⁸⁴ *Id.*; *see also* Van Bogaert and Storch, *supra* note 79, at 236.

⁸⁵ Either Signet Banking Corporation or its wholly-owned subsidiary, Signet Bank, formerly employed the plaintiffs. *Franklin*, 84 F. Supp. 2d at 721. For simplicity, this paper will refer to these two business entities as “Signet Bank.”

⁸⁶ The defendants were First Union Corporation, a bank holding company; First Union National Bank, a wholly-owned subsidiary of First Union Corporation; Capital Management Group, a division of First Union National Bank; the First Union Corporation Savings Plan, a 401(k) savings plan organized for First Union Corporation’s employees nationwide; and the First Union Savings Plan Administration Committee, the plan administrator of the First Union Corporation Savings Plan. *Id.* at 721-22.

⁸⁷ *Id.* at 726. This allegation is contained in Count III of the Complaint. *Id.*

⁸⁸ *Id.* This allegation is contained in Count IV of the Complaint. *Id.* Count I of the Complaint alleged that the amendment to the Signet 401(k) plan (merging it with the First Union Plan) was not adopted in conformity with the documents governing the Signet 401(k) plan, and was therefore void. *Id.* Count II alleged that even if the amendment was valid, the Signet 401(k) plan terminated and did not merge with the First Union 401(k) plan. *Id.* Count V alleged that certain Signet Plan participants did not receive notice or received inadequate notice of the changes to the Signet Plan and their right to opt out of these changes. *Id.*

⁸⁹ *Franklin v. First Union Corp.*, No. 99-CV-610 (E.D. Va. filed September 7, 1999) (hereinafter “*Franklin II*”). The defendants in *Franklin II* were First Union Corporation, First Union Savings Plan Administration Committee, First Union National Bank, and First Union Corporate Savings Plan. *Id.*, Comp.

second lawsuit included claims that First Union engaged in self-dealing⁹⁰ and that benefits of the plan improperly inured⁹¹ to First Union⁹² because the only investment alternatives offered were those proprietary to First Union.

The defendants moved for summary judgment on all of the allegations in *Franklin I*, except the allegation that they breached their fiduciary duties by liquidating the investment alternatives in the Signet Plan.⁹³ The district court granted the First Union Defendants partial summary judgment, specifically holding that the participants did not have a vested right to the investment alternatives in the Signet Plan.⁹⁴ The court relied on a Treasury regulation excluding “the right to a particular form of investment (e.g., investment in employer stock or securities or investment in certain types of securities, commercial paper, or other investment media)”⁹⁵ as an accrued benefit under ERISA that could not be reduced or altered.⁹⁶ The court further noted that responsibility for selecting investment alternatives rested with the plan fiduciaries, who had both the responsibility and authority under Department of Labor regulations to remove investment alternatives.⁹⁷ The court reasoned that because the § 404(c) regula-

⁹⁰ *Id.*, Comp. ERISA § 406(b), 29 U.S.C. § 1106(b) (2002) provides: “A fiduciary with respect to a plan shall not deal with the assets of the plan in his own interest or for his own account.”

⁹¹ *Franklin II*, *supra* note 89, Comp. ERISA § 403(c) provides: “[T]he assets of a plan shall never inure to the benefit of any employer and shall be held for the exclusive purposes of providing benefits to participants in the plan and their beneficiaries and defraying reasonable expenses of administering the plan.” ERISA § 403(c), 29 U.S.C. § 1103(c) (2002).

⁹² These allegations were resolved as part of the global settlement of both *Franklin I* and *Franklin II*. See *Franklin II*, *supra* note 89, Settlement, at <http://firstunionsuit.com/Settlement.html> (last visited April 28, 2002). Allegations similar to those made in *Franklin II* were made in *Mehling v. New York Life Insurance Co.*, 163 F. Supp. 2d 502 (E.D. Pa. 2001). In *Mehling*, the court granted defendant New York Life summary judgment on plaintiffs’ claims that it breached its fiduciary duty by providing only investment alternatives in its own proprietary funds. 163 F. Supp. 2d at 502. The court held that while ERISA § 406 “prohibits fiduciaries from involving plan assets in various acts of self-dealing or conflicts of interest,” a specific exemption from these rules issued by the Secretary of Labor applied to New York Life’s investments in its proprietary funds. *Id.* at 510 (discussing Prohibited Transaction Exemption 77-3). Further discussion of the *Franklin II* case is beyond the scope of this article.

⁹³ The First Union Defendants later moved for summary judgment as to Count IV of the Complaint. *Franklin v. First Union Corp.*, Memorandum in Support of Defendants’ Motion for Summary Judgment on Count IV, p. 4, at http://www.signetsuit.com/Defendant_Count_IV_Brief.doc (last visited April 28, 2002).

⁹⁴ *Franklin v. First Union Corp.*, 84 F. Supp. 2d 720, 736 (E.D. Va. 2000). The court also granted Defendants summary judgment on Counts I and II and denied them summary judgment on Count V. *Id.*; see *supra* notes 87-88 (describing allegations contained in these Counts).

⁹⁵ Treas. Reg. § 1.411(d)-4(A-1)(d)(7) (2002).

⁹⁶ *Franklin*, 84 F. Supp. 2d at 731. Under ERISA’s “anti-cutback rule” an accrued benefit “may not be decreased by an amendment of the plan.” ERISA § 204(g), 29 U.S.C. § 1054(g)(1) (2001).

⁹⁷ *Franklin*, 84 F. Supp. 2d at 731-32. Under the preamble to the § 404(c) regulations, promulgated by the Department of Labor, the plan fiduciary has the obligation “to determine . . .

tions place the responsibility on the plan fiduciary for periodically evaluating the various investment alternatives that are available to participants in a § 404(c) plan, the “plan fiduciary has the responsibility for selecting investment alternatives and, by definition, has authority to remove alternatives.”⁹⁸ Finally, the court relied on the Signet Plan’s express language allowing addition and deletion of investment alternatives to the plan.⁹⁹

The court did not address whether First Union breached a fiduciary duty by liquidating the Signet employees’ investments in the Signet Plan when it was merged with the First Union Plan because the First Union Defendants did not move for summary judgment on this issue.¹⁰⁰ Interestingly, however, the court noted that, despite its grant of summary judgment to the *First Union* defendants on Count III (alleging a vested right to the investment alternatives in the Signet Plan), such a ruling “does not . . . foreclose plaintiffs’ claims in Count IV that the defendants breached their fiduciary duties in liquidating participants’ investments in the Signet Plan and discontinuing the non-proprietary investment options.”¹⁰¹ Prior to any ruling by the court on the First Union Defendants’ later motion for summary judgment on Count IV of the Complaint, the lawsuit was settled.¹⁰²

IV. ANALYSIS OF THEORIES OF FIDUCIARY RESPONSIBILITY ADVOCATED BY *FIRST UNION* PLAINTIFFS

The *First Union* plaintiffs’ claims, while possessing an inherent common-sense and fairness appeal, should be rejected in favor of a bright line standard that a plan sponsor does not become a fiduciary when it merges 401(k) plans in the context of a larger corporate merger without considering the investment alternatives in an acquired corporation’s 401(k) plan.

whether the [investment alternatives] should continue to be available as participant investment options.” 57 Fed. Reg. 46906, 46924 n.27 (Oct. 12 1992).

⁹⁸ *Franklin*, 84 F. Supp. 2d at 732.

⁹⁹ *Id.* at 732-33. The Signet Plan stated: “The Committee may add to or reduce the number and type of Investment Funds that will be available for investment in any Plan Year. The Committee shall select the Investment Funds in accordance with ERISA section 404(c) and the regulations thereunder.” *Id.* at 732 (quoting Signet Banking Corporation Employee Savings Plan § 8.3(b)).

¹⁰⁰ *Id.* at 726. Defendants later moved for summary judgment with respect to Count IV of the Complaint. See *supra* note 93.

¹⁰¹ *Franklin*, 84 F. Supp. 2d at 733 n.6.

¹⁰² Morton A. Harris, *Working with Participant Directed Investments Under ERISA § 404(c)*, SGO08 A.L.I.-A.B.A. 887, 939 (2001); see also Signet Plan Litigation Website, at <http://www.signetsuit.com> (last visited March 17, 2002).

The federal courts have considered several factors in determining the meaning and scope of ERISA. First, courts have looked to its plain language.¹⁰³ Specifically, courts have examined the structure of the Act as a whole when construing its language, although simultaneously cautioning against reading the requirements of one section into another because separate sections may have had different purposes or Congressional concerns when enacted.¹⁰⁴ As part of their examination of the structure of ERISA, courts have attempted to read and interpret it to ensure internal consistency.¹⁰⁵ Second, Courts have been loath to impose extra-textual remedies under ERISA because of its carefully balanced and comprehensive remedial scheme.¹⁰⁶

Third, courts have looked to the legislative history of ERISA, specifically, Congress's public policy concerns in enacting ERISA. While Congress's overarching purpose for the Act was to protect employee pension plans, Congress also wished to encourage employers to establish pension plans and was concerned that over-regulation of the plans would discourage employers from doing so.¹⁰⁷ Courts have therefore been wary of proposed interpretations or constructions of ERISA that would create a burden on employers, especially where they would not otherwise advance ERISA's beneficent purposes.

A. *Plain Language of the Act*

1. Interpreting ERISA's Fiduciary Duties in Light of the Structure of the Act

A person who selects investment alternatives for a participant-directed 401(k) plan acts in a fiduciary capacity and must conform that activity to ERISA's fiduciary standards because of the functional nature of the definition of "fiduciary" under ERISA.¹⁰⁸ Other sections of ERISA, however, specifically set out the requirements for merging plans.¹⁰⁹ Because these different duties are in

¹⁰³ See *infra* Part IV.A; *Mass. Mut. Life Ins. Co. v. Russell*, 473 U.S. 134, 148 (1985) (interpreting ERISA in light of "the relevant text . . . the structure of the entire statute, and its legislative history.").

¹⁰⁴ See *Curtiss-Wright Corp. v. Schoonejongen*, 514 U.S. 73, 84 (1995) ("[W]e do not think Congress intended [one part of the statute] to be supplemented by a faraway provision in another part of the statute, least of all in a way that would lead to improbable results."); *Mass. Mut. Life*, 473 U.S. at 148.

¹⁰⁵ *Mass. Mut. Life*, 473 U.S. at 148.

¹⁰⁶ See *infra* note 124 and Part IV.B.

¹⁰⁷ See *infra* Part IV.C.1.

¹⁰⁸ See *supra* note 7.

¹⁰⁹ ERISA § 208 provides: "A pension plan may not merge or consolidate with . . . any other plan . . . unless each participant in the plan would (if the plan then terminated) receive a benefit immediately after the merger . . . which is equal to or greater than the benefit he would have been entitled to receive immediately before the merger." ERISA § 208, 29 U.S.C. § 1058 (2001).

different parts of the Act, they should not be read as modifying each other.¹¹⁰ Indeed, ERISA § 208, the section specifying the requirements for merging plans, contains a specific exemption if participants are covered by a multiemployer plan governed by subchapter III of ERISA.¹¹¹ That is, Congress specifically exempted multiemployer plans from the general merger requirements. Had Congress likewise wanted to make exceptions from or impose duties other than those specifically enumerated in § 208—including imposing fiduciary duties upon plan sponsors—it could have done so.¹¹²

2. Interpreting ERISA to Avoid Internal Inconsistency with Respect to Participants' Rights to Investment Alternatives

The court in *Franklin v. First Union Corp.* specifically held that the former Signet Plan participants had no vested right to the investment alternatives in the Signet Plan.¹¹³ A holding that a plan sponsor has a fiduciary duty to investigate investment alternatives in an acquired company's 401(k) plan, however, will *de facto* create such a right. If the investment alternatives in the acquired corporation's 401(k) are outperforming the current investment alternatives in the acquirer's 401(k), the fiduciary will feel compelled to examine the acquired corporation's investment alternatives and add them to the investment alternatives already existing in the acquirer's plan. Failure to do so would lead to allegations that the fiduciary did not examine the investment alternatives consistent with fiduciary duties.¹¹⁴ This allegation would have almost immediate credence in a circumstance (like the one present in *First Union*) where the in-

¹¹⁰ The United States Supreme Court has previously used such a structural analysis of ERISA's various sections to hold that different sections of ERISA should not be read as overlapping unless Congress clearly intended them to do so. See *Curtiss-Wright Corp. v. Schoonejongen*, 514 U.S. 73, 84 (1995) ("This may not be a foolproof informational scheme, although it is quite thorough. Either way, it is the scheme that Congress devised. And we do not think Congress intended it to be supplemented by a faraway provision in another part of the statute, least of all in a way that would lead to improbable results."); see also *Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 51 (1987) (construing ERISA and stating: "in expounding a statute, we must not be guided by a single sentence or member of a sentence, but look to the provisions of the whole law, and to its object and policy").

¹¹¹ ERISA § 208, 29 U.S.C. § 1058 ("The preceding sentence shall not apply to any transaction to the extent that participants either before or after the transaction are covered under a multiemployer plan to which subchapter III of this chapter applies."); see *supra* note 45 (describing generally functions of subchapter III of ERISA).

¹¹² *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 97 (1983) ("We must give effect to this plain language unless there is good reason to believe Congress intended the language to have some more restrictive meaning.").

¹¹³ See *supra* notes 94-99 and accompanying text (discussing district court's holding that former Signet employees had no vested right to investment alternatives in the Signet Plan).

¹¹⁴ See *supra* note 7 (describing fiduciary duties of persons selecting investment alternatives in ERISA § 404(c) plan); *supra* Part II.B (describing fiduciary standards in general).

vestment alternatives at issue were outperforming those in the acquirer's plan. A fiduciary facing such allegations—where the damages can already be calculated as the difference between the better-performing investment of the acquired company and the performance of the existing funds of the acquirer company—may add the funds simply to avoid litigation and potential damages.

Although discussing welfare benefits,¹¹⁵ the Sixth Circuit addressed a similar argument in *Adams v. Avondale Industries, Inc.*¹¹⁶ In that case, several former employees sued Avondale Industries, claiming, *inter alia*, that its attempted amendment of an unwritten severance plan was invalid because “Congress intended to foreclose amendment or termination of all benefit plans except where such action would be in the interests of plan participants.”¹¹⁷

The court rejected the plaintiffs' argument, explaining that Congress specifically chose not to require vesting of welfare benefits because the costs of such vesting would discourage employers from establishing welfare benefit plans. The court reasoned:

In drawing the line between employer actions subject to the fiduciary duty requirement and those not, we must avoid any rule that would have the effect of undermining Congress' considered decision that welfare benefit plans not be subject to a vesting requirement. We are compelled, therefore, to reject plaintiffs' proposed rule that welfare benefit plans such as the one before us be amended or terminated only when such action would be in the best interests of the employees. *To adopt such a requirement would, in effect, accord employees a vested right to welfare benefits, thereby upsetting ERISA's delicate balance in this area.* Instead, we employ the rule . . . that a company does not act in a fiduciary capacity when deciding to amend or terminate a welfare benefits plan.¹¹⁸

¹¹⁵ ERISA defines an “employee welfare benefit plan” as

any plan, fund, or program . . . established or maintained by an employer . . . for the purpose of providing for its participants or their beneficiaries . . . medical, surgical, or hospital care or benefits, or benefits in the event of sickness, accident, disability, death or unemployment, or vacation benefits, apprenticeship or other training programs, or day care centers, scholarship funds, or pre-paid legal services.

ERISA § 3(1), 29 U.S.C. § 1002(1) (2001). Welfare benefit plan administrators are required to comply with ERISA's fiduciary requirements and reporting and disclosure requirements, but are exempted from the participation, funding, and vesting sections of ERISA. ERISA §§ 201, 301, 29 U.S.C. §§ 1051, 1081 (2001); *Adams v. Avondale Indus., Inc.*, 905 F.2d 943, 947 (6th Cir. 1990).

¹¹⁶ 905 F.2d 943 (6th Cir. 1990).

¹¹⁷ *Id.* at 946.

¹¹⁸ *Id.* at 947 (emphasis added).

As the Sixth Circuit held in *Avondale Industries* with respect to welfare benefits, creating a *de facto* right by expanding the plan sponsor's duties in a merger would undermine ERISA's lack of a vesting requirement for investment alternatives.¹¹⁹

Moreover, such a right would have several negative effects that would conflict with other fiduciary duties under ERISA. First, requiring the fiduciary to consider (and likely implement) another investment alternative simply because it is currently performing well in the marketplace will interfere with the fiduciary's duty to ensure diversity in the investment alternatives and would create additional burdens of administration in attempting to comply with the ERISA § 404(c) regulations.¹²⁰ The fiduciary is already under a duty to examine the appropriateness of the investment alternatives in the acquirer's portfolio on a regular basis to ensure that they are proper.¹²¹

Second, requiring the fiduciary to examine an acquired corporation's investment alternatives would make this activity subject to the happenstance event of corporate activity. That is, if a company happens to merge, then the fiduciary is saddled with the additional burden of reviewing the acquired company's 401(k) investment alternatives temporally proximate to the merger. Of course, the fiduciary may have recently reviewed the investment alternatives of the acquirer company or may plan to do so in the near future as part of his duty to review the investment alternatives periodically to ensure that they continue to meet the ERISA § 404(c) regulation requirements.¹²² If subject to ERISA's fiduciary standards, the merger would require further examination of other alternatives in addition to the usual activity of the fiduciary. Such extra examination of investment alternatives would not depend on ERISA or any Department of Labor regulation; rather, it would depend solely on whether the corporation happened to merge at a given time. Following this line of logic, a corporation that happened to merge three times in one year would have to examine the investment alternatives offered to participants three times more than would a corporation that did not merge at all during the year. This contravenes the certainty, predictability, and uniformity that Congress sought to achieve through passage of ERISA.¹²³

¹¹⁹ See *supra* notes 94-99 and accompanying text (discussing holding by district court in *First Union* that ERISA does not provide plan participants with a vested right to investment alternatives).

¹²⁰ See *supra* Part II.A.4 (describing range of investment alternatives that must be available for participants and beneficiaries under a plan that wishes to comply with ERISA's 404(c) "safe harbor" regulation).

¹²¹ See *supra* note 7.

¹²² See *id.*

¹²³ *Alessi v. Raybestos-Manhattan, Inc.*, 451 U.S. 504, 523 (1981) ("Congress intended . . . to establish pension plan regulation as exclusively a federal concern."); H.R. REP. NO. 93-533, at 12 (1973), *reprinted in* 1974 U.S.C.C.A.N. 4639, *reprinted in* 2 SENATE COMMITTEE ON LABOR AND PUBLIC WELFARE, LEGISLATIVE HISTORY OF ERISA, 94th Cong., 2d Sess., 2359 (Comm. Print

B. Courts' Reluctance to Impose Additional Remedies Under ERISA

Courts are loath to impose extra-textual remedies¹²⁴ because of the detailed remedial scheme promulgated under ERISA.¹²⁵ Adopting the *First Union* plaintiffs' argument that ERISA's fiduciary duties apply to plan mergers would impose such an extra-textual remedy. If an employer chooses to comply with

1976) ("The uniformity of decision which the Act is designed to foster will help administrators, fiduciaries and participants to predict the legality of proposed actions without the necessity of reference to varying state laws.").

¹²⁴ *Mass. Mut. Life Ins. Co. v. Russell*, 473 U.S. 134, 145 (1985) ("The federal judiciary will not engraft a remedy on a statute, no matter how salutary, that Congress did not intend to provide."); *id.* at 146-47 ("The six carefully integrated civil enforcement provisions found in §502(a) of the statute as finally enacted, however, provide strong evidence that Congress did *not* intend to authorize other remedies that it simply forgot to incorporate expressly. . . . We are reluctant to tamper with an enforcement scheme crafted with such evident care as the one in ERISA."); *Trans-america Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 19 (1979) ("[W]here a statute expressly provides a particular remedy or remedies, a court must be chary of reading others into it.").

The United States Supreme Court's decision in *Harris Trust & Savings Bank v. Salomon Smith Barney Inc.*, 530 U.S. 238 (2000), is consistent with this principle. In *Harris Trust*, a trustee of a pension plan sought to rescind a sale of motel properties between the plan and Salomon, despite Salomon's status as a non-fiduciary under ERISA. 530 U.S. at 243. The trustee also sought restitution of the purchase price and disgorgement of any profits made by Salomon on the transaction. *Id.* The Court held that ERISA § 502(a)(3)'s authorization of "appropriate equitable relief" allowed the trustee to seek such equitable relief from a non-fiduciary. *Id.* at 241. In so holding, the Court first noted that "ERISA's 'comprehensive and reticulated' scheme warrants a cautious approach to inferring remedies not expressly authorized by the text." *Id.* at 247 (internal citations omitted). The Court found, however, that this type of equitable relief against a non-fiduciary was, in fact, authorized by the text of the Act. *Id.* at 247 ("In this case, however, §502(l) resolves the matter—it compels the conclusion [that the above-described relief was appropriate against a non-fiduciary]."); *see also id.* at 247-49 (examining statutory text).

Moreover, the primary questions before the respective courts in *Harris Trust* and *First Union* were dissimilar. In *Harris Trust*, the Court addressed whether a non-fiduciary was an appropriate defendant under ERISA § 502(a)(3). *Id.* at 241 ("The question [before the Court] is whether [§ 502(a)(3)'s authorization of appropriate equitable relief] extends to a suit against a non-fiduciary [party]."). No allegation was made in *Harris Trust* that Salomon was a fiduciary, as that term is defined in ERISA.

In *First Union*, the plaintiffs asked a fundamentally different question: whether a non-fiduciary (a plan settlor) became a fiduciary when it merged two participant-directed 401(k) plans. In other words, *Harris Trust* asked, "is a non-fiduciary a proper defendant?" while *First Union* asked, "When does a person become a fiduciary in the context of the merger of participant-directed 401(k) plans?"

See Great-West Life & Annuity Ins. Co. v. Knudson, 534 U.S. 204, 221 (2002) (holding that where plaintiffs sought "legal relief—the imposition of personal liability on respondents for a contractual obligation to pay money," plaintiffs were not seeking "equitable relief" and hence *Harris Trust* was inapplicable).

¹²⁵ ERISA § 409, 29 U.S.C. § 1109 (2001) (describing liability of person for breach of fiduciary duty under ERISA); ERISA § 502, 29 U.S.C. § 1132 (2001) (describing civil enforcement of ERISA provisions).

the Department of Labor's § 404(c) regulations, ERISA promises participants investment alternatives with certain characteristics from which participants may choose.¹²⁶ The *First Union* plaintiffs, however, did not ask for a fund with investment alternatives that complied with the ERISA § 404(c) regulations (which they nonetheless received when they were allowed to participate in the First Union Plan). Rather, they asked for the right to a portfolio of their own choosing: one that included funds they felt would yield superior performance. Providing participants a right to demand a portfolio of their own choosing—and allowing them to recover damages for the failure to provide it—is providing a remedy not contemplated by ERISA for denial of a benefit that ERISA does not recognize.

Notably, the former Signet employees were still protected by ERISA. In compliance with the § 404(c) regulations, First Union had to offer participants at least three investment alternatives that were diversified individually and in the aggregate, that provided participants an opportunity to materially affect the return and risk on their accounts, and that allowed the participants to diversify their investments and thereby minimize the risk of large losses.¹²⁷ That is, the participants were provided with an opportunity to invest in alternative investments that both Congress and the Department of Labor felt were appropriate under the circumstances. Failure on the part of First Union to offer such an array of appropriate investments would have resulted in the First Union Plan not qualifying under § 404(c)¹²⁸ and potential liability for failure to meet such regulations.¹²⁹ The fiduciary provided participants with a periodic review of the investment alternatives offered as part of his duty to ensure that the array of available alternatives continued to meet the regulations.¹³⁰ Accordingly, the Signet Plan participants were already sufficiently protected to ensure that Congress's and the Department of Labor's mandates concerning investment of retirement funds were met. The *First Union* plaintiffs simply sought to add another protection and another remedy to that which ERISA already provides.

¹²⁶ See *supra* Part II.A.4 (describing requirements of investment alternatives offered to participants under an ERISA § 404(c) plan).

¹²⁷ 29 C.F.R. § 2550.404c-1(b)(3) (2002).

¹²⁸ *Id.* § 2550.404c-1(a)(2) (“The standards set forth in this section are applicable solely for the purpose of determining whether a plan is an ERISA section 404(c) plan.”).

¹²⁹ Failure to meet the requirements of § 404(c) regulations would mean that the trustee would otherwise be liable for any losses caused by breach of his fiduciary duties. ERISA § 409, 29 U.S.C. § 1109 (2001).

¹³⁰ See *supra* note 7.

C. *Purposes of ERISA*

1. **Balancing ERISA's Goals of Protecting Employee Pension Plans with Its Desire to Encourage Employers to Establish Such Plans**

The central purpose of Congress in passing ERISA was to protect employees' pension plans.¹³¹ Congress, however, also wished to encourage employers to sponsor pension plans for their employees.¹³² Should courts interpret ERISA's fiduciary duties to include plan mergers, they would violate both these Congressional purposes.

First, such an interpretation would not enhance Congress's central purpose of protecting employee pension plans. As discussed above, the former Signet Plan participants were still protected by ERISA and were provided all rights that ERISA guarantees under the § 404(c) regulations. Second, such an interpretation would defeat Congress's companion purpose of encouraging employers to establish employee pension plans. By creating additional administrative burdens and exposure to large litigation damages in the event of a merger, courts would discourage employers from establishing or maintaining pension plans for their employees. An interpretation so at odds with two of the central purposes of ERISA is not plausible.

¹³¹ ERISA § 2(b), 29 U.S.C. § 1001(b) (2001) ("It is hereby declared to be the policy of this chapter to protect interstate commerce and the interests of participants in employee benefit plans and their beneficiaries, by requiring the disclosure and reporting to participants and beneficiaries of financial and other information with respect thereto, by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing for appropriate remedies, sanctions, and ready access to the Federal courts.").

¹³² *Varity Corp. v. Howe*, 516 U.S. 489, 497 (1996) (stating that in interpreting ERISA's fiduciary duties, "courts may have to take account of competing congressional purposes, such as Congress' desire to offer employees enhanced protection for their benefits, on the one hand, and, on the other, its desire not to create a system that is so complex that administrative costs, or litigation expenses, unduly discourage employers from offering welfare benefit plans in the first place.") (citations omitted); *Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 54 (1987) ("[T]he detailed provisions of § 502(a) set forth a comprehensive civil enforcement scheme that represents a careful balancing of the need for prompt and fair claims settlement procedures against the public interest in encouraging the formation of employee benefit plans."); *Mass. Mut. Life Ins. Co. v. Russell*, 473 U.S. 134, 148 n.17 (1985) ("Indeed, Congress was concerned lest the cost of federal standards discourage the growth of private pension plans."); *Alessi v. Raybestos-Manhattan, Inc.*, 451 U.S. 504, 515 (1981) ("[T]he House Ways and Means Committee expressly acknowledged the tension between the primary goal of benefiting employees and the subsidiary goal of containing pension costs.").

2. Providing a Uniform Interpretation of Employer Duties and Employee Rights with Respect to Pension Plans

Another purpose of ERISA is to provide a uniform set of rules and regulations to govern pension plans.¹³³ Granting the *First Union* plaintiffs their interpretation of the statute does not foster uniformity, but rather leaves fiduciary duties to the whim of the stock market. Depending on whether the stock or fund in the acquired company's 401(k) plan is up or down in the market on a given day will in large part determine whether a fiduciary duty exists to consider that investment alternative as part of the merger of the employee pension plans. If an investment alternative in the acquired company's portfolio is not performing as well as the investment alternatives in the acquiring company's portfolio, it is unlikely that participants would question a fiduciary's rejection of such fund.¹³⁴ On the other hand, if an investment alternative out-performs one or more of the investment alternatives in the acquiring company's portfolio, participants would likely claim that the fiduciary had a duty to consider such funds. Because one of the important goals of ERISA is to provide a comprehensive statute that deals uniformly with pension plans and fiduciary duties, leaving the existence of such duties to the capricious nature of the marketplace is less than idealistic. Indeed, the facts of the *First Union* case illustrate this admonition. If the First Union-Signet merger occurred one year later, the investment alternatives that the former Signet Plan participants attempted to recapture via litigation would have under-performed the investment alternatives in the First Union Plan.¹³⁵

V. CONCLUSION: TERMINATION OF INVESTMENT ALTERNATIVES IN MERGED 401(K) PLANS IS NOT SUBJECT TO ERISA'S FIDUCIARY DUTIES

In light of these customary guideposts for construction of ERISA, courts should reject arguments labeling a plan sponsor as a fiduciary simply because the sponsor eliminates an acquired corporation's 401(k) investment alternatives in merging the sponsor's 401(k) with the plan of the acquired corporation. Courts should instead establish a bright-line rule that there is no fiduciary activity on the part of the plan sponsor via such conduct.

The simplicity of the *First Union* plaintiffs' proposed interpretation of ERISA, which would require plan sponsors to act as fiduciaries when merging

¹³³ See *supra* note 123.

¹³⁴ A fiduciary is liable to the plan only for losses or damages caused to the plan that result from the breach of the fiduciary's duties. ERISA § 409(a), 29 U.S.C. § 1109 (2001) ("[A] fiduciary . . . who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries . . . shall be personally liable to make good to such plan any losses to the plan *resulting from each such breach.*") (emphasis added).

¹³⁵ Franklin v. First Union Corp., Memorandum in Support of Defendants' Motion for Summary Judgment on Count IV, pp. 12, 16, at http://www.signetsuit.com/Defendant_Count_IV_Brief.doc (last visited April 28, 2002).

401(k) plans, is inherently appealing. The *First Union* plaintiffs asked only that First Union, as plan sponsor, look at the Signet Plan's funds and their performance prior to unilaterally eliminating them. If such funds were not appropriate, then they could be eliminated as investment options; on the other hand, if such funds were superior to those offered in the First Union Plan, what reason would First Union have for not wanting its employees to have the benefit of such superior-performing funds?

What this argument has in simplicity, however, it lacks in substance. The perceived substantive evil of a plan sponsor not being required to examine a merger partner's 401(k) investment alternatives is just that: perceived. ERISA promises neither a perfect selection of 401(k) investment alternatives nor one of the participant's choosing; indeed, ERISA promises no retirement plan at all. ERISA instead promises that if the plan sponsor wishes to comply with the § 404(c) regulations, the trustee must provide a diversified portfolio of investment alternatives; the Signet Plan members received exactly that upon participation in the First Union Plan. Courts should reject the *First Union* plaintiffs' proposed interpretation of ERISA's fiduciary rules and hold that no fiduciary duty exists on the part of the plan sponsor when it merges participant-directed 401(k) accounts, even when it cancels investment alternatives in the merged plan without examination of those alternatives. Such a bright-line standard will prevent an interpretation of ERISA that creates an oppressive and complex body of rules in the context of corporate merger; confusion and inconsistency for employers, employees, and other plan officials with respect to their rights and duties in a merger; and voluminous litigation for all.

