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Arbitration of ERISA Claims Part II: Courts Continue to Grapple with Competing Considerations

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This column previously considered the issue of whether the Employee Retirement Income Security Act ("ERISA") allowed plans to require arbitration of ERISA claims ("Part I").[1] Part I discussed the competing views of the U.S. Court of Appeals for the Ninth Circuit in *Dorman v. Charles Schwab Corp.* ("*Dorman II*")[2] and a lower court from the U.S. District Court for the Northern District of Illinois in *Smith v. Greatbanc Tr. Co.*[3]

As Part I noted at the time, *Smith* was pending before the U.S. Court of Appeals for the Seventh Circuit. Since then, the Seventh Circuit issued its decision in *Smith v. Board of Directors of Triad Mfg., Inc.*, affirming the lower court's decision.[4] However, as discussed below, the Seventh Circuit's reasoning differs slightly from the lower court in at least one significant respect that is supportive of the idea that ERISA claims can be arbitrated. But in other respects, the Seventh Circuit's decision points to some possible limits on what plan sponsors may require be arbitrated.

The upshot is continued uncertainty that plan sponsors will have to navigate to the extent they wish to require arbitration of ERISA claims.

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Background on Arbitration Generally

By way of reminder, whether arbitration can, as a general matter, be required is fully endorsed by the Federal Arbitration Act's[5] "liberal federal policy favoring arbitration agreements" because it can provide employees and employers "quicker, more informal, and often cheaper resolutions" of workplace-related disputes.[6] The question remains, however, whether that general endorsement of arbitration has been "overridden by a contrary congressional command,"[7] by any provision of ERISA. The answer to that question points to some of the remaining tension between the *Dorman* and *Triad* decisions.

Dorman II *Holds ERISA Claims may Broadly be Arbitrated*

As discussed in Part I, the Ninth Circuit in *Dorman II* endorsed a broad right of plan sponsors to require arbitration, both in terms of the breadth of that requirement and the ease by which participants can be deemed to have consented to arbitration.

To recap, the plaintiff in *Dorman* participated in Schwab's 401(k) plan which, after he left Schwab's employment, was amended to include an arbitration provision.[8] The provision required binding arbitration of any "claim, dispute or breach arising out of or in any way related" to the plan.[9] It also barred class or multi-participant claims.[10]

After leaving Schwab, the plaintiff filed an ERISA class action alleging various claims for breach of fiduciary duty and violations of ERISA's prohibited transactions rules.[11] In response, the defendants moved to compel arbitration, which the lower court denied. It reasoned, *inter alia*, that prior Ninth Circuit precedent precluded arbitration because class action waivers were deemed unenforceable.[12]

On appeal, *Dorman v. Charles Schwab Corp.* ("*Dorman I*")[13] addressed the threshold question of whether ERISA claims could be subject to mandatory arbitration.[14] The Ninth Circuit acknowledged that it had previously held in *Amaro v. Continental Can Co.*[15] that "ERISA mandated 'minimum standards [for] assuring the equitable character of [ERISA] plans' that could not be satisfied by arbitral proceedings."[16] However, *Dorman I* recognized that its prior skepticism had been addressed by subsequent Supreme Court decisions that held "arbitrators are competent to interpret and apply federal statutes."[17] Accordingly, the Ninth Circuit held *Amaro* was no longer binding precedent.[18]

The Ninth Circuit in *Dorman II* then addressed whether arbitration should be compelled. The Ninth Circuit held that the district court erred in several respects. As an initial matter, and as is relevant here to our discussion of the Seventh Circuit's *Smith* decision, the Ninth Circuit held that the district court incorrectly concluded that the plaintiff was not

bound by the Plan's arbitration provision.[19] The Ninth Circuit noted that the plaintiff participated in the plan for almost a year after the arbitration provision was enacted.[20] And "[a] plan participant agrees to be bound by a provision in the plan document when he participates in the plan while the provision is in effect."[21]

In addition, and again as is relevant to the analysis below of the Seventh Circuit's decision, the Ninth Circuit held that although ERISA Section 502(a)(2) claims seek relief on behalf of the plan, "such claims are inherently individualized when brought in the context of a defined contribution plan like that at issue."[22] And since the plaintiff and the plan agreed to arbitration on an individualized basis, the plan's "waiver of class-wide and collective arbitration must be enforced according to its terms."[23]

Smith *Holds Some ERISA Claims may be Arbitrated*

The Smith Lower Court Finds the Arbitration Provision Invalid

As discussed in Part I, the lower court in *Smith v. Greatbanc Tr. Co.*[24] found that the plaintiff's claims were not subject to arbitration. In *Smith*, the plaintiff participated in an employee stock ownership plan ("ESOP") which, while the plaintiff was employed, had a broad arbitration clause. And, like the one in *Dorman*, it prohibited any group, class or collective arbitrations.[25]

After the plaintiff filed a suit alleging various breaches of fiduciary duty, the defendants moved to compel arbitration. The plaintiff argued, among other things, that the arbitration provision was invalid because he did not consent to its inclusion, and because, it prevented him from pursuing plan-wide remedies under ERISA Section 502(a)(2).[26]

On the consent issue, the *Smith* court found that the defendants did not attempt to show the presence of any contract formation elements; namely, offer, acceptance or consideration.[27] As such, it rejected defendants' argument, based on *Dorman II*, that "continued participation in a plan is the equivalent of any agreement to any plan amendments,"[28] particularly in the absence of any evidence plaintiff had been notified of the amendment that added the arbitration provision.[29]

On the scope of remedies argument, the *Smith* court found that the arbitration provision impermissibly restricted plaintiff to only pursuing individualized relief, notwithstanding the fact that ERISA Section 502(a)(2) allowed individuals to sue for plan-wide relief.[30] In so holding, the *Smith* court disagreed with the Ninth Circuit's conclusion in *Dorman II* that such an outcome was aligned with the Supreme Court's decision in *LaRue*.[31] According to the *Smith* court, *LaRue* did not "suggest that an individual plan participant's claim can somehow be split from a claim seeking plan-wide relief."[32] The *Smith* court,

therefore, did "not see how plan-wide relief could be achieved in individual arbitration . . . which . . . limits claimants to 'individual relief.'"[33]

The Seventh Circuit Affirms by Focusing on the Scope of Remedies Point

On its review of the foregoing facts, the Seventh Circuit affirmed the district court's holding.[34] The Seventh Circuit noted the case presented "complicated" facts[35] but found the "correct resolution" of the case to be "straightforward."[36] In short, and as explained in greater detail below, Triad's arbitration requirement failed because it "precludes relief that 'has the purpose or effect of providing additional benefits or monetary or other relief to any Eligible Employee, Participant or Beneficiary" other than the plaintiff.[37] However, the Seventh Circuit did acknowledge that, the following textual impairment aside, nothing in ERISA precluded arbitration agreements as a general proposition.[38]

The Seventh Circuit began its analysis by reviewing the purpose of ERISA Section 1109.[39] The Seventh Circuit explained that Supreme Court precedent made it clear that the purpose of Section 1109 was to provide "plan-wide," as opposed to individual, relief.[40]

Relatedly, the Seventh Circuit discussed the significance of whether an ERISA claim involved a defined benefit or defined contribution plan.[41] The court noted that *Russell* involved a defined benefit plan, so its discussion of "plan-wide" relief "'speaks to the impact of § [1109] on plans that pay defined benefits.'"[42] But because the "landscape of employee benefits plans" had changed, the Seventh Circuit explained that *LaRue* further held that a fiduciary's misconduct "'need not threaten the solvency of the of the entire plan," in order for a claim involving a defined contribution plan to fall "'squarely within' § 1109."[43]

Having previewed the foregoing framework for permissible ERISA claims, the Seventh Circuit proceeded to the threshold question of whether such claims as a general matter could be arbitrated.[44] Based on the Federal Arbitration Act and substantial Supreme Court precedent, the Seventh Circuit had little difficulty concluding they were.[45] In this regard, the Seventh Circuit's analysis departs from the lower court's skepticism that such claims could be arbitrated.

Elaborating on its holding, the Seventh Circuit explained that, given Congress' strong endorsement of arbitration and the absent of any "'contrary congressional command' precluding arbitration" of ERISA claims," the Seventh Circuit held that "ERISA claims are generally arbitrable."[46] In this regard, the Seventh Circuit is fully aligned with the Ninth Circuit's decision in *Dorman I*, which the Seventh Circuit cited in support of its conclusion.[47]

However, despite this alignment, the Seventh Circuit further concluded that Triad's arbitration provisions were not enforceable.[48] The

Seventh Circuit explained its holding emanated from the "effective vindication" exception the Supreme Court explored in *American Express Co. v. Italian Colors Restaurant*.[49] As the Seventh Circuit explained, prior Supreme Court precedent "'asserted the existence of an 'effective vindication' exception,'" that as a matter of public policy, would invalidate an arbitration agreement that prevented a party from asserting their statutory rights.[50]

While describing the exception as "rare," the Seventh Circuit found it applied to Triad's arbitration agreement.[51] This is because the "plan's arbitration provision, which also contains a class action waiver, precludes a participant from seeking or receiving relief that 'has the purpose or effect of providing additional benefits or monetary or other relief to any Eligible Employee, Participant or Beneficiary other than" [the plaintiff].[52] And certain relief allowed under ERISA Section 1109, such as a removal of a fiduciary, was prohibited by Triad's arbitration agreement.[53]

Given the foregoing, the Seventh Circuit found an irreconcilable conflict between Section 1109 and the limits in Triad's arbitration agreement.[54] Because Triad's agreement operated as a prospective waiver of remedies allowed by ERISA, the Seventh Circuit concluded the "effective vindication" exception barred enforcement of the agreement.[55] The Seventh Circuit succinctly explained its view: "the problem with the plan's arbitration provision is its prohibition on certain plan-wide remedies, not plan-wide representation."[56]

In reaching this holding, the Seventh Circuit addressed the defendants' reliance on *Dorman II*.[57] Notably, the Seventh Circuit saw no conflict with its ruling and *Dorman II because* the *Dorman* arbitration provision "lacked the problematic language present here."[58] Thus, in the Seventh Circuit's view, unlike *Dorman,* the relief requested by the plaintiff in *Triad* (e.g., removal of the fiduciary) "cannot have anything *but* a plan-wide effect."[59] In that regard, the Seventh Circuit, contrary to the *Triad* defendants' assertions, did not find an ERISA/FAA conflict.[60] Instead, the conflict "was between ERISA and the plan's arbitration provision, which precludes certain remedies that §§ 1132(a)(2) and 1109(a) expressly permit."[61]

The Seventh Circuit concluded its analysis, by outing several "limits" and "lessons" from its holding. Specifically, it expressed no view on:

- Whether the plaintiff consented to the arbitration provision (an issue expressly resolved in *Dorman*);
- Whether the plaintiff received notice of the arbitration provisions (an issue resolved at least implicitly in *Dorman*);
- Whether the plan sponsor could unilaterally amend the plan to insert an arbitration provision (an issued expressly resolved in *Dorman*); and

- What other ERISA relief (e.g., under 29 U.S.C. § 1132(a)(3), as opposed to under 29 U.S.C. § 1132(a)(2)) *may* be barred by an arbitration provision.

Where Does all This Leave Arbitration of ERISA Claims?

The good news, as discussed above, is that the Seventh Circuit has aligned itself with the Ninth Circuit and "every other circuit to consider the issue,"[62] on whether ERISA claims, as a general matter, can be arbitrated. This may have resolved at least some of the conflict between *Dorman* and the lower court's decision in *Smith* that we discussed in Part I. However, as noted above, the Seventh Circuit did not address issues regarding notice, consent and plan amendment, all of which may impact the introduction of an arbitration provision into an existing plan document. We think *Dorman* is correct that plan participants must be bound by plan amendments even absence evidence of consent. But obviously, other courts may view this issue differently. So stay tuned.

The other tension that may remain between the Ninth and Seventh Circuits' analyses involves the "scope of remedies" issue. As discussed in Part I, there is clear tension between how this issue was approached by the Ninth Circuit and the lower court in *Smith*. The Seventh Circuit suggested the outcome in *Dorman* was driven by different plan language. But as we discussed before, there is a broader tension in legal analyses that may not turn on the particular plan language.

In addition, and contrary to *Dorman*, other courts continue to conclude that adequate consideration or express participant consent are necessary for such claims to be arbitrated.[63] Thus, plan sponsors will have to continue to consider the jurisdictions where their plan is administered, or the location of plan participants, in evaluating the risk of trying to add an arbitration requirement to an existing plan.

Plan sponsors and employers also need to make sure that the language they rely upon to require arbitration is sufficiently broad to cover ERISA claims.[64] Careful drafting is yet another important consideration as employer and plan sponsors continue to weigh the pros and cons of requiring arbitration of ERISA claims.

Notes

1. M. Hlousek and J. Torres, Arbitration of ERISA Claims – Courts Continue to Grapple with Competing Considerations, 47 *Employee Relations L.J.* No. 1 (Summer 2021).

2. *Dorman v. Charles Schwab Corp.*, 780 Fed. Appx. 510 (9th Cir. 2019).

3. *Smith v. Greatbanc Tr. Co.*, No. 20 C 2350, 2020 WL 4926560 (N.D. Ill. Aug. 21, 2020).

4. *Smith v. Board of Directors of Triad Mfg., Inc.*, 13 F.4th 613 (2021).

5. 9 U.S.C. §§1-16.

6. *Epic Sys. Corp. v. Lewis*, 138 S.Ct. 1612, 1621 (2018). *See also American Express Co. v. Italian Colors Restaurant*, 570 U.S. 229 (2013).

7. *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 226 (1987).

8. *Schwab*, 934 F.3d at 1109.

9. *Id.*

10. *Id.* at 1009-10.

11. *Id.*

12. *Id.* at 1111 (citing *Morris v. Ernst & Young, LLP*, 834 F.3d 975 (9th Cir. 2016), reversed by *Epic Sys. Corp. v. Lewis*, 138 S. Ct. 1612 (2018)).

13. *Dorman v. Charles Schwab Corp.*, 934 F.3d 1107 (9th Cir. 2019).

14. *Id.* at 1109.

15. *Amaro v. Continental Can Co.*, 724 F.3d 747 (9th Cir. 1984).

16. *Dorman I*, 934 F.3d at 1111 (quoting *Amaro*, 724 F.2d at 752).

17. *Id.*, 934 F.3d at 1111 (citing *Italian Colors*, 570 U.S. at 233).

18. *Dorman I*, 934 F.3d at 1112.

19. *Dorman II*, 780 F. App'x 512-13.

20. *Id.*

21. *Id.* at 513 (citing *Chappel v. Lab. Corp. of Am.*, 232 F.3d 719, 723-24 (9th Cir. 2000)).

22. *Dorman II*, 780 F. App'x at 514 (citing *LaRue v. DeWolff, Boberg & Assocs., Inc.*, 552 U.S. 248 (2008)).

23. *Dorman II*, 780 F. App'x at 514 (quoting *Italian Colors* 570 U.S. at 233).

24. *Smith v. Greatbanc Tr. Co.*, No. 20 C 2350, 2020 WL 4926560 (N.D. Ill. Aug. 21, 2020), aff'd *Smith v. Board of Directors of Triad Mfg, Inc.*, 13 F.4th 613 (2021).

25. *Id.*

26. *Id.*

27. *Smith*, 2020 WL 4926560 at *2.

28. *Id.* at *3.

29. *Id.*

30. *Smith*, 2020 WL 4926560 at *4.

31. *Id.*

32. *Id.*

33. *Id.*

34. *Smith v. Board of Directors of Triad Mfg, Inc.*, 13 F.4th 613 (2021).

35. *Id.* at 615.

36. *Id.*

37. *Id.*

38. *Id.* at 619-620.

39. *Id.* at 618 (citing 29 U.S.C. § 1109(a)).

40. *Id.* at 618-19 (citing *Massachusetts Mutual Life Ins. Co. v. Russell*, 473 U.S. 134, 136, 139-44 (1985) and *LaRue v. DeWolff, Boberg & Assoc., Inc.*, 552 U.S. 248, 250-51, 253-56 (2008).

41. *Triad*, 13 F.4th at 619.

42. *Id.* at 619 (quoting *Russell*, 473 U.S. at 255).

43. *Id.* (quoting *LaRue*, 552 U.S. at 253, 256).

44. *Id.* at 619.

45. *Id.* at 619-20 (citations omitted).

46. *Id.* at 620 (citations omitted).

47. *Triad*, 14 F.4th at 620 (citing *Dorman I*, 934 F.3d at 1112) (other citations omitted).

48. *Id.* at 620.

49. *American Express Co. v. Italian Colors Restaurant*, 570 U.S. 228, 235 (2013).

50. *Triad*, 13 F.4th at 621 (quoting *Italian Colors*, 570 U.S. at 235-36) (other citations omitted).

51. *Triad*, 13 F.4th at 621.

52. *Id.*

53. *Id.*

54. *Id.*

55. *Id.* at 622 (citations omitted).

56. *Id.*

57. *Id.*

58. *Id.* at 622-23 (citing *Dorman v. Charles Schwab & Co. Inc.*, No. 17-cv-00285-CW, 2018 WL 467357, at *2 (N.D. Cal. Jan. 18, 2018)).

59. *Triad*, 13 F.4th at 622.

60. *Id.*

61. *Id.* at 622-23.

62. *Triad*, 13 F.4th at 620.

63. *E.g., Brown on behalf of Henny Penny Corp. Employee Stock Ownership Plan v. Wilmington Tr., N.A.*, No. 3:17-cv-250, 2018 WL 354186, at *5 (S.D. Ohio July 24, 2018) (rejecting premise that fiduciary could unilaterally require arbitration of breach of fiduciary duty claims because it would be akin to "allowing the fox to guard the henhouse")

(quoting *Munro v. Univ. of S. California*, 2017 WL 1654075, at *6 (C.D. Cal. Mar. 23, 2017)); *Hensiek v. Board of Directors of Casino Queen Holding Co., Inc.*, 514 F.Supp.3d 1045, 1053-54 (S.D. Ill. 2021), on appeal, No. 21-1175 (7th Cir.) (while plan gave board of directors authority to amend plan, inclusion of new arbitration requirement failed for lack of consideration).

64. *E.g., Cooper v. Ruane Cunniff & Goldfarb Inc.*, 990 F.3d 173, 182-83 (2d Cir. 2021) (agreement to arbitrate claims "relating to employment" did not cover ERISA claims).