

The LaRue Decision and Missing Participants: Impact for 401k Plan Sponsors, Human Resources and Participants

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The recent decision of the Supreme Court in *LaRue v. DeWolff, Boberg & Associates Inc.*, 128 S. Ct. 1020 (2008) (“LaRue”) is a landmark ruling that will be referenced in employee benefits law text books for years to come.

James LaRue filed a suit, alleging that by failing to execute his investment selection, DeWolff and the Plan breached their fiduciary duties. Under the Employee Retirement Income Security Act of 1974 (ERISA), section 502(a)(2), he subsequently sought to recover the amount he lost due to that failure. Ultimately, it was the Supreme Court’s decision to side with LaRue, not the Plan.

As a result of the Court ruling, any single participant in a defined contribution plan now has a cause of action under ERISA if fiduciary misconduct causes a loss to his or her account. This brings to light the need for greater care to be taken in how plan assets are invested and administered, and even more important that missing participants are being managed throughout the life cycle of the plan.

The Risks of Missing Participants

Missing participants present a risk for potential fiduciary liability that was largely overlooked prior to the ruling. In order to avoid this increasingly detected risk, plan administrators must:

- Maintain proper communication of required information
- Ensure a valid investment election is always on file and in effect
- Manage appropriate death benefit distribution to beneficiary

The plan administrator’s obligation to meet communication requirements for all participants is a challenge especially for the “missing”.

While participants are active participants, communications may be made in electronic form as long as the general participant population has access to computers. But once a participant is no longer active, notices must be sent in hard copy. This becomes difficult when the record keeper or third party administrator (TPA) no longer has a current address for an inactive participant.

The second area of potential risk involves the investment of plan assets. Virtually all 401(k) plans rely on ERISA section 404(c) to insulate plan fiduciaries from responsibility for a participant’s investment selections. However, in order for fiduciaries to be protected, it is required that that each participant has a valid investment election in effect. For active participants, the investment election may be made electronically and the participant can be reminded periodically to make sure that the election is up-to-date. However, this notification cannot be accomplished if the participant is missing. Potential for fiduciary liability arises even though the plan fiduciary may think that he is protected.

A third area of potential risk relates to death benefit distributions. One of the principal reasons why inactive participants go missing is because they have died and the plan was not notified. Under all 401(k) plans the death of the participant is a distribution event. This means that the plan administrator has an obligation to locate the deceased participant's beneficiary and to make a distribution of the deceased participant's account to that beneficiary. This obligation will not be satisfied if the plan does not know that the participant has died. Thus, if the participant's account diminishes in value between the date of death and the date when the death benefit is eventually paid, it may be the plan administrator who is liable for that loss.

Failure to comply with any of these requirements can and will result in a fiduciary liability, particularly if the account balance is adversely affected.

Risk Management – Locating Missing Participants

With the LaRue decision confirming the potential for having fiduciary liability arise from the existence of missing participants, plan sponsors and administrators must give some serious thought as to how to better manage the risks associated with missing participants.

The best method of risk management in this area is to periodically review the plan's participant data base in search of "missing" participants and to take immediate steps to locate those individuals. It is well known that the longer a participant has been removed from his or her employer, the harder it is to have accurate contact information and the harder it is to find that participant if current contact information is not available. Keeping track of participants must be done on a routine basis in order to be successful. To manage risk, it is critical for plan sponsors and administrators to adopt procedures that will minimize the number of missing participants.