

# Employee Benefit ■ Plan Review

## The Law on ERISA Plan Arbitration Provisions Remains Unsettled

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Courts continue to disagree over the enforceability of mandatory arbitration provisions containing class action waivers set forth in benefit plans governed by the Employee Retirement Income Security Act of 1974 (ERISA).

Despite a split among the circuit courts, the U.S. Supreme Court has declined to hear challenges to decisions issued by the U.S. Court of Appeals for the Third and Tenth Circuits, finding the mandatory class action waivers contained in the plans' arbitration provisions were unenforceable because they purportedly interfered with participants' alleged statutory rights to pursue relief on behalf of all absent plan participants and their individual plan accounts.

Although several district courts have denied motions to compel individual arbitration in recent months, the most recent court to rule on this – the U.S. District Court for the Eastern District of Kentucky – granted the defendants' motion to compel individual arbitration, finding that a plan's arbitration provision and class action waiver must be enforced. Relying on precedent from the U.S. Court of Appeals for the Sixth Circuit and from the U.S. Supreme Court, the district court rejected the plaintiffs' argument that enforcing the arbitration agreement's class action waiver would "prospectively waive" their statutory rights. The court ultimately held that an arbitration agreement does not impact substantive

statutory rights but "merely changes how those rights will be processed."

### SUPREME COURT DECLINES TO HEAR TWO CASES, RULING THAT MANDATORY INDIVIDUAL ARBITRATION PROVISIONS ARE UNENFORCEABLE

In October 2023, the Supreme Court declined certiorari petitions to hear cases from the U.S. Court of Appeals for the Third and Tenth Circuits, which had declined to enforce mandatory arbitration and class action waiver clauses in plan documents.

In *Harrison v. Envision Mgmt. Holding Inc. Bd. of Dir.*,<sup>1</sup> the plaintiff-plan participant asserted six causes of action, including claims under ERISA Sections 502(a)(2) and (a)(3), and sought plan-wide relief, including, among other things, a declaration that all defendants breached their fiduciary duties, the removal of the employee stock ownership plan (ESOP) trustee and the restoration of the ESOP's losses resulting from the breach of fiduciary duties. The plan contained an arbitration provision with a class action waiver that required the plaintiff to arbitrate his claims on an individual basis.

The Tenth Circuit affirmed the district court's application of the judge-made "effective vindication" doctrine to find that the plan's arbitration provision was unenforceable.<sup>2</sup> The

“effective vindication” doctrine is an exception to the Federal Arbitration Act (FAA) that seeks to balance the competing federal policies in enforcing arbitration agreements and vindicating the plaintiffs’ rights to pursue statutory remedies. The *Harrison* court recognized that “[a]lthough the Supreme Court has repeatedly recognized the existence of the effective vindication exception, it has, to date, declined to actually apply the exception in any case before it.”<sup>3</sup>

## The Tenth Circuit affirmed the district court’s application of the judge-made “effective vindication” doctrine to find that the plan’s arbitration provision was unenforceable.

Nevertheless, the Tenth Circuit affirmed the district court’s application of the doctrine to hold “that the arbitration provision acts as a prospective waiver” of the plaintiff’s right to pursue statutory remedies under ERISA “because it disallows plan-wide relief, which is expressly contemplated by [Sections 1132(a)(2) and 1109 of] ERISA.”<sup>4</sup>

The Third Circuit in *Henry v. Wilmington Trust NA* applied a similar analysis to reach the same conclusion.<sup>5</sup> The court noted that “[b]ecause the class action waiver purports to prohibit statutorily authorized remedies, the class action waiver and the statute cannot be reconciled.”<sup>6</sup> The court thus held that the class action waiver was unenforceable and declined to compel arbitration.

In petitioning for a review by the Supreme Court, the defendants in these cases argued that the appellate courts “ignored” or “sidestepped” relevant precedent and improperly read into ERISA a substantive,

unwaivable right to bring plan-wide representative ERISA claims on behalf of absent plan participants or their individual plan accounts. By doing so, the petitions argued that the courts created “disharmony” between ERISA and the FAA, which requires courts to enforce arbitration agreements according to their terms. The petitions also argued that the lower courts failed to consider the implications of the Supreme Court’s decision in *Viking River Cruises Inc. v. Moriana*,<sup>7</sup> which held that representative claims that seek to join together the claims of individual claimants can be prohibited in the face of a provision that requires individual arbitration.

## The district court disagreed with plaintiffs and concluded that the plan’s class action waiver language was enforceable.

The Supreme Court declined to certify either case for review. It may be that the Supreme Court is waiting for additional courts to weigh in on this issue, and decisions are expected out of the U.S. Court of Appeals for the Second, Fifth and Sixth Circuits by the end of the summer of 2024.

### EASTERN DISTRICT OF KENTUCKY ENFORCES MANDATORY CLASS ACTION WAIVER AND ARBITRATION PROVISION IN ESOP PLAN DOCUMENT

Despite several district courts relying on the reasoning of the *Harrison* and *Henry* decisions, a recent decision by the U.S. District Court for the Eastern District of Kentucky compelled plaintiffs-participants to individually arbitrate their ERISA claims.

In *Merrow v. Horizon Bank*,<sup>8</sup> the plaintiffs-employees brought a putative class action against Horizon Bank, the fiduciary trustee for the ESOP, and two selling shareholders,

alleging that the trustee significantly overvalued the employer stock purchased by the ESOP and caused the ESOP to purchase the stock from the selling shareholders for above fair market value. The plaintiffs alleged that this transaction ultimately caused them and the ESOP to lose money.

The defendants moved to dismiss the case for lack of subject matter jurisdiction, arguing in relevant part that the class action waiver provision divested the court of subject matter jurisdiction and required the court to compel individual arbitration.<sup>9</sup>

The relevant provision of the arbitration agreement read:

No Class Arbitration or Class Relief. Each Participant and Beneficiary, or any party claiming for or through them, agrees that any Claims will be arbitrated individually and shall not be brought, heard, or arbitrated on a class or collective action basis – unless both parties agree, in writing, to the contrary.<sup>10</sup>

In response, the plaintiffs invoked the “effective vindication doctrine,” claiming that the class action waiver was unenforceable because it operates as a “prospective waiver” of plaintiffs’ statutory right to seek plan-wide relief under ERISA Section 502(a)(2).<sup>11</sup>

The district court disagreed with plaintiffs and concluded that the plan’s class action waiver language was enforceable. The court noted that Sixth Circuit precedent and the FAA imposes a presumption in favor of arbitration and resolves all doubts in favor of arbitration. To that end, the court found that the plaintiffs failed to carry their burden of establishing that the plan document’s class action waiver is invalid and unenforceable. Rejecting their argument that the “effective vindication” doctrine should apply, the court cited *Viking River Cruises* and reasoned that “[a]n arbitration agreement thus does not alter or abridge substantive rights; it merely changes how those rights

will be processed.”<sup>12</sup> The court then clarified that the right of a participant to seek relief on behalf of an entire plan, including absent plan participants and their accounts, is a procedural right (as opposed to a substantive right) that can be waived through individual arbitration provisions.

#### IN SUMMARY

- Courts continue to disagree over the enforceability of mandatory arbitration provisions containing class action waivers set forth in benefit plans governed by ERISA.
- In the absence of U.S. Supreme Court resolution, uncertainty will persist regarding the validity and enforceability of individual arbitration provisions in ERISA plans.

- Plan sponsors should expect to see more litigation over the arbitrability of ERISA Section 502(a)(2) claims in the near term, and thoughtfully drafted arbitration provisions are key to minimizing the risk of potential class action litigation.

#### CONCLUSION

In the absence of Supreme Court resolution, uncertainty will persist regarding the validity and enforceability of individual arbitration provisions in ERISA plans. Plan sponsors should expect to see more litigation over the arbitrability of ERISA Section 502(a)(2) claims in the near term.

In light of this continued uncertainty, thoughtfully drafted arbitration provisions are key to minimizing

the risk of potential class action litigation. 🌐

#### NOTES

1. 59 F.4th 1090, 1112 (10th Cir. 2023), cert. denied sub nom., 2023 WL 6558426 (U.S. Oct. 10, 2023).
2. Id. at 1112.
3. Id. at 1098.
4. Id. at 1096.
5. 72 F.4th 499 (3d Cir. 2023), cert. denied sub nom., 2023 WL 6797729 (U.S. Oct. 16, 2023).
6. Id. at 507.
7. *Viking River Cruises Inc. v. Moriana*, 142 S. Ct. 1906 (2022).
8. 2023 WL 7003231 (E.D. Ky. Oct. 24, 2023).
9. Id. at \*3.
10. Id.
11. Id. at \*6.
12. Id.

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