

## Publications

# 401(k) Plan Forfeitures – The Department of Labor Backs Employers in Arguing that Lawsuit Should Be Dismissed

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## PUBLISHED

07/14/2025

## SOURCE

Groom Publication

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In a [July 9<sup>th</sup> amicus brief](#) filed with the Ninth Circuit Court of Appeals, the Department of Labor (“DOL”) weighed in on the wave of 401(k) lawsuits – over 65 cases have been filed – challenging how forfeitures are used in 401(k) plans. The Ninth Circuit is the first appellate court being asked to rule on the topic. Backing the defendant company and plan administrator, DOL argued that allegations that a plan fiduciary operates under a conflict of interest in administering forfeitures and that the plan fiduciary should use forfeitures to pay administrative expenses, rather than offset employer contributions, are insufficient to state a viable claim under ERISA.

It is noteworthy that the Ninth Circuit case, [Hutchins v. HP, Inc.](#), involves a plan document that extends a good deal of flexibility as to the use of forfeitures. It states that forfeitures “may be used to reduce employer contributions, to restore benefits previously forfeited, to pay Plan expenses, or for any other permitted use.” In other words, the plan describes different options and does not require forfeitures first be used to pay plan expenses.

At the outset of its brief, DOL helpfully reinforced that there has been an “established understanding for several decades ...that defined contribution plans...may allocate forfeited employer contributions to pay benefits for remaining participants rather than using those funds to defray administrative expenses.” DOL also argued that “the fundamental problem” with the plaintiff’s theories is that “they ignore the constraints on the fiduciary’s decision-making” and “misunderstand[] the boundary between settlor and fiduciary functions.”

More specifically, DOL argued that the funding of a plan, including decisions regarding the timing and amount of contributions, is a “settlor function,” not a fiduciary function actionable under ERISA. And, while the act of actually allocating forfeitures is a fiduciary function because it amounts to an exercise of control over plan assets, DOL described that the added context that funding remains a settlor decision supports the conclusion that allocating forfeitures to fund employer contributions does not give rise to a claim for breach of fiduciary duty, especially when that use is an option expressly identified in the plan document.

DOL also discussed that certain risks that “are eliminated where the fiduciary chooses to use the forfeitures to cover the remaining matching contribution amount.” Specifically, it noted that the plaintiff “ignore[d] other considerations” relative to the use of forfeitures, such as:

If the HP Plan Committee chose to use forfeitures to pay plan expenses rather than fund matching contributions, then the HP Plan Committee would need to ask the sponsor to contribute more funds to the plan to cover the outstanding and unpaid matching contributions. If the sponsor refused, then the plan would be faced with a funding shortfall and unable to timely allocate matching contributions to each participant as required by the plan terms. The fiduciary would then need to engage in a potentially protracted legal dispute, using plan assets, to try to obtain the full amount of matching contributions from the sponsor. The risks of a dispute between the fiduciary and the plan sponsor are appropriately factored into a fiduciary’s assessment of which course of action best satisfies its duties of loyalty and prudence.

**GROOM INSIGHT:** The DOL’s amicus brief aligns with congressional history and Treasury Department guidance that has allowed forfeitures to be used to offset employer contributions for more the 60 years. It is a welcome development for plan sponsors concerned about litigation risk and is particularly helpful because it was filed in a case where the plan language provided an unfettered choice among a number of different potential uses of forfeitures, which is a common plan provision. The DOL brief likely will be heavily cited in the other pending forfeitures cases.

Groom attorneys work closely with sponsors and fiduciaries to help them understand the implications of litigation trends and identify tools to mitigate risk. Given the ongoing litigation over forfeitures, plan sponsors may want to review their plan provisions to ensure that both the sponsor’s intent and administrative practices are aligned and appropriately reflected.