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Seventh Circuit Vacates Class Certifications in 401(k) Fee Cases

On January 21, 2011, the U.S. Court of Appeals for the Seventh Circuit vacated class certification orders in the 401(k) fee cases brought against Boeing and International Paper. *Spano v. The Boeing Co.*, -- F.3d --, 2011 WL 183974 (7th Cir. 2011). As discussed below, the Court concluded that participants in 401(k) plans do not necessarily share common interests and, in fact, their interests may conflict depending on, among other things, the investment options in which they invested and the timing of those investments.

Background

The plaintiffs in the fee cases are participants in their employer-sponsored 401(k) plans. As in other fee lawsuits, the participants claim that the companies, and certain committees and employees, breached their fiduciary duties under ERISA by (1) causing the plan to pay excessive fees and expenses, (2) including imprudent investment options in the plan, and (3) concealing from plan participants material information regarding the plan fees and expenses and plan investment options.

A lawsuit can proceed as a class action if all of the requirements of Rule 23(a) and one of the requirements of Rule 23(b) are satisfied. The requirements of Rule 23(a) are: (1) the class members are so numerous that joinder of all members is impracticable; (2) there are common questions of law or fact; (3) the claims or defenses of the named plaintiffs (class representatives) are typical of the claims or defenses of the other class members; and (4) the named plaintiffs will fairly and adequately protect the interests of the class.

Assuming the Rule 23(a) requirements are satisfied, Rule 23(b) identifies three potential avenues for class certification. The Court focused on Rule 23(b)(1) which permits class certification if prosecuting separate individual actions would create the risk of: (A) establishing incompatible standards of conduct for the defendants through multiple court decisions; or (B) court decisions that, as a practical matter, would be dispositive of the interests of the "other members not parties to the [court decisions] or would substantially impair or impede their ability to protect their interests."

In the fee cases against Boeing and International Paper, the district court (S.D. Ill.) certified the following class of plaintiffs under Rule 23(a) and Rule 23(b)(1) of the Federal Rules of Civil Procedure –

All persons, excluding the Defendants and/or other individuals who are or may be liable for the conduct described in this Complaint, who are or were participants or beneficiaries of [the plan] and who are, were or may have been affected by the conduct set forth in this Complaint, as well as those who will become participants or beneficiaries of [the plan] in the future.

The Seventh Circuit's Decision

Rule 23(a)

While the Seventh Circuit noted that numerosity was not contested and that plaintiffs were alleging common questions – *e.g.*, that the plan included imprudent investment options, and that the fees charged to the participants were unreasonable – the Court concluded that the class definition failed to meet Rule 23(a)'s other requirements of typicality and adequacy-of-representation.

As to the typicality requirement, the Court found that the named plaintiffs' claims may not be typical because the plaintiffs and other class members may have invested in different investment options. *Id.* at *11 ("[W]e think that[, at a minimum,] there must be a congruence between the investments held by the named plaintiff and those held by members of the class he or she wishes to represent."). The Court also commented that individualized questions as to whether a particular participant relied on an alleged misrepresentation might preclude a finding of typicality, at least where the alleged misrepresentation is not "so central to the operation of a plan that injury may be shared." *Id.* at *14.

As to the adequacy-of-representation requirement, the Court found that the interests of the named plaintiffs and other class members may differ because the named plaintiffs and other class members may have invested in a particular investment option at different times. The Court observed that the named plaintiffs' interests actually could be adverse to the interests of some of the other class members who had no complaints about particular investment options.

Rule 23(b)(1)

The Seventh Circuit also found that the class definition failed to meet the requirements of Rule 23(b)(1). First, the Court saw "no reason to assume" that an adjudication of one person's claim would be dispositive of the interests of the other class members or would substantially impair or impede their ability to protect their interests. In this respect, the Court recognized that "[a] claim of imprudent management . . . is not common if the alleged conduct harmed some participants and helped others." *Id.* at *12.

Second, the Court noted that individual actions may not give rise to a risk of "inconsistent or varying adjudications that might establish incompatible standards of conduct for the defendant[s]." *Id.* The Court explained that defendants could comply with varying adjudications regarding whether a particular investment option should be offered to a subset of participants by dividing the plan into one or more sub-plans, only some of which include the investment option.

Class Certification Is Still Possible

The Seventh Circuit did not rule out the possibility that the district court could certify an appropriate class on remand. The Court noted that the "logic of *LaRue* compels the conclusion that there might be plan losses in a defined-contribution setting, and at least some of those losses might be of the type that do not vary from participant to participant." *Id.* at *10. Accordingly, it is possible that the district court may certify one or more classes based on whether a group of participants invested in a particular fund at approximately the same times.

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In this regard, the Court noted that a fiduciary could be liable for selecting an improper investment option, even where the participants make the decision whether to invest in that option. That said, the Seventh Circuit suggested that, even if a proper class can be defined, it may be difficult for plaintiffs to prevail on the merits where the plan includes numerous other investment options. *Id.* at *14.

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