

Court Declines to Dismiss Suit Alleging ERISA Violations by 401(k) Plan Sponsor That Used Plan Forfeitures to Reduce Employer Contributions

EBIA Weekly (October 3, 2024)

[*Rodriguez v. Intuit, Inc.*, 2024 WL 3755367 \(N.D. Cal. 2024\)](#)

A federal trial court has rejected a 401(k) plan sponsor's motion to dismiss a participant's lawsuit alleging that the plan sponsor and administrative committee breached their fiduciary duties of loyalty and prudence and engaged in anti-inurement and prohibited transactions by using plan forfeitures to reduce future employer contributions instead of offsetting administrative expenses charged to individual accounts. The plan's terms gave the plan sponsor discretionary authority over forfeiture management, specifically providing that forfeited nonvested accounts "could be used," at the plan sponsor's election, either to cover administrative expenses or to reduce future matching or profit-sharing contribution obligations. Here are highlights of the court's opinion:

- **Fiduciary Status.** Because the plan's provisions gave the plan sponsor discretion to decide whether and how much of the forfeitures to allocate toward employer matching and profit-sharing contributions, the court ruled that the plan sponsor functioned as a fiduciary, and not as a settlor, when applying forfeitures. The plan's terms also provided that the administrative committee, as the named fiduciary, appointed the plan sponsor to fulfill fiduciary responsibilities under the plan with respect to any forfeiture allocations. This discretionary responsibility over the management of forfeitures rendered the plan sponsor a fiduciary.
- **Loyalty and Prudence.** Analyzing various plan provisions addressing fee payments, expense management, and forfeiture allocations, the court concluded that the plan sponsor had discretion to determine how to allocate forfeitures, and the participant had sufficiently alleged that the plan sponsor had breached its duty of loyalty by making decisions that were not in participants' best interest. The court also found persuasive the participant's argument that the plan sponsor violated the terms of the plan because the plan prohibited the use of forfeitures to offset anything other than safe harbor matching and profit-sharing contributions, yet the employer contributions that the forfeitures allegedly were allocated to cover did not match either definition. Furthermore, the participant plausibly alleged that the plan sponsor had violated ERISA's duty of prudence by failing to engage in a reasoned and impartial decision-making process that considered all relevant factors before determining how to use the forfeited funds.
- **Inurement and Self-Dealing.** Addressing the participant's claim that the plan sponsor had received a benefit equal to millions of dollars of debt forgiveness by electing to use plan assets to reduce future contributions, the plan sponsor argued that the claim was incompatible with IRS and DOL regulations

allowing the allocation of forfeitures to cover employer contributions. But the court pointed out that, while the regulations would generally permit employers to structure plans to allow forfeitures to cover contributions, they did not establish that the plan sponsor's actions within the parameters of this specific plan were permissible or lawful. The court ultimately concluded that the participant had plausibly stated a claim for unlawful employer inurement because she had shown that the plan sponsor used assets for a purpose other than to pay its obligations to plan beneficiaries. Furthermore, the participant plausibly pleaded that the plan sponsor's reallocation of forfeitures benefited itself to the detriment of the plan by reducing the funds available to participants and for investment, thereby creating a plausible inference that the plan sponsor had engaged in self-dealing.

EBIA Comment: This is one of several California cases in which participants have sued 401(k) plans for using forfeitures to offset future employer contributions instead of covering administrative expenses charged to individual accounts. As noted by the court, DOL and IRS regulations permit forfeitures to be used to pay administrative expenses, reduce future employer contributions, or make additional employer contributions. The issue is the plan language granting the plan sponsor the "discretion to choose" among these methods. If the plan had instead provided that all forfeitures would first be used to reduce employer contributions and then to pay plan expenses, the plan sponsor would have acted in a ministerial manner without exercising discretion, and a claim alleging ERISA violations would likely fail. Note that these cases are only at preliminary stages of litigation; it's uncertain whether a court will ultimately rule in participants' favor. For more information, see EBIA's 401(k) Plans manual at Sections IX.E ("Allocation of Forfeitures"), XXIV.E ("ERISA Fiduciary Duties") and XXXVII ("Special Issues: ERISA Litigation"). See also EBIA's ERISA Compliance manual at Section XVI.C ("ERISA's Exclusive Benefit Rule").

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