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Employee Benefit Plan Review

Thinking ESOPs: Fourth Circuit Narrows Equitable Relief Under ERISA

By Rick Pearl

In *Rose v. PSA Airlines, Inc.*,[1] the U.S. Court of Appeals for the Fourth Circuit held that ERISA Section 502(a)(3), which permits a claim for "other appropriate equitable relief," does not allow claims to recover money from a defendant's general assets. This article discusses the *Rose* decision and its potential impact on employee stock ownership plan (ESOP) cases.

The Issue

Congress drafted ERISA to focus largely on those who make final, discretionary decisions about plan management, administration or assets. These are the "fiduciaries," and they are bound by ERISA's prohibited- transactions provisions, duties of prudence and loyalty, and other fiduciary requirements. ERISA also has requirements for non-fiduciaries, including disclosure obligations, claims-processing obligations and others.

Generally speaking, ERISA does not govern the conduct of non-fiduciaries, or of third parties who are not plan administrators, claims handlers or sponsoring/participating employers.

ERISA's enforcement provisions, which contain ERISA's exclusive list of authorized claims or causes of action, have a similar focus. ERISA creates a cause of action for benefits due – Section 520(a)(1)(B) – that typically is brought against a plan, plan administrator, or claims handler, and a cause of action against a fiduciary to recover loss to plan caused by a fiduciary breach – Section 502(a)(2).

There is a "catchall" cause of action in Section 502(a)(3) that allows a participant, beneficiary or fiduciary to sue to enjoin violations of ERISA or a plan or obtain "other appropriate equitable relief" to remedy a breach of ERISA or plan, or enforce ERISA or the terms of a plan.[2] The Supreme Court has held that a Section 502(a)(3) claim can be brought against any category of defendants – it does not need to be a fiduciary, plan, plan administrator or claims handler.

In litigation involving ESOP transactions, Section 502(a)(3) is the cause of action that plaintiffs use to bring claims against a selling shareholder. A common claim against a selling shareholder in an ESOP transaction will allege that the seller "knowingly participated" in a prohibited transaction and received more than fair market value for the stock. Some plaintiffs in ESOP transaction cases will seek a variety of supposedly equitable remedies, such as surcharge, disgorgement, a constructive trust, an equitable lien, and recission of the ESOP transaction.

Courts have struggled with interpreting Section 502(a)(3) and deciphering its requirements and limitations. The Supreme Court has made clear in several decisions that Section

502(a)(3) only permits equitable claims for equitable relief – i.e., both the claim and the relief must be equitable – and the term “equitable” refers to remedies that “typically” were available when courts were separated into courts of law and courts of equity. There have not been separate courts of law in equity in U.S. federal courts since 1938, and the distinction was abolished in England in the early 1800s. There are entire treatises written about the difference between legal remedies and equitable remedies and about the history of the divided courts, but understanding the difference is complicated, and something most lawyers never have to deal with in their careers.

The question before the Fourth Circuit in *Rose* dealt with the nature of the plaintiff’s claims and requested relief – were they equitable, or were they legal?

The *Rose* Decision

Rose involved an ERISA lawsuit alleging that defendants improperly denied a claim for health-plan benefits. The plaintiff, who sued on behalf of her son, brought a Section 502(a)(3) claim to recover the monetary cost of her son’s heart surgery, which she alleged was wrongfully denied, along with a claim to recover “unjust enrichment” to the defendants for wrongfully retaining money that should have paid for the heart surgery.

The court first addressed the claim to recover the monetary cost of the heart surgery. Although it is common for people to think that a monetary remedy automatically is legal, and not equitable, in nature, the difference between a legal remedy and an equitable remedy is not as simple as a money versus non-money.

Historically, courts of equity could award various types of money relief that were equitable in nature. For example, the remedy of “equitable compensation” or “surcharge,” which was essentially a monetary award from a defendant’s general assets, was an equitable remedy that equity courts would award in cases where equity courts had exclusive jurisdiction over a dispute, such as trust disputes that could be brought only in equity courts.

But the fact that some relief could be awarded by a court of equity is not enough to establish that the relief itself was traditionally available in equity. Courts of equity also had “concurrent jurisdiction” with the courts of law over certain types of cases. The distinction between exclusive jurisdiction and concurrent jurisdiction was vital to the Fourth Circuit, because exclusive jurisdiction cases were not traditional cases, but unusual ones. To determine what relief was traditionally available in courts of equity, the Fourth Circuit looked at cases where courts of equity had concurrent jurisdiction, not exclusive jurisdiction.

The remedies that were available in concurrent-jurisdiction cases were different from remedies available in exclusive-jurisdiction cases. Surcharge was available in trust cases, where an equity court had exclusive jurisdiction, and thus it was not a remedy that was “typically” available. Thus, the plaintiff’s Section 502(a)(3) claim to recover the amount of the heart surgery, which was akin to a claim for equitable compensation or surcharge, failed as a matter of law and had to be dismissed.

The plaintiff’s claim for unjust enrichment was different. Unjust enrichment was an available remedy in concurrent- jurisdiction cases. Thus, it was traditionally available in courts of equity, and available under ERISA Section 502(a)(3). An unjust enrichment claim requires a plaintiff to prove, that a “person is unjustly enriched because the retention of [a] benefit would be unjust.” If the benefit happened to be money (as opposed to some other type of property), equity courts could award equitable restitution by requiring the “wrongfully obtained” money to be returned to its rightful owner. The court explained that “[a] plaintiff alleging unjust enrichment can get a monetary remedy under ERISA only if she seeks specific funds that are wrongfully in the defendant’s possession and rightfully belong to her. Courts cannot award her relief that amounts to personal liability paid from the defendant’s general assets to make the plaintiff whole.”

Furthermore, a plaintiff must plead plausible grounds in a complaint to obtain unjust enrichment under ERISA. This requires a plaintiff “to identify the specific property (funds) that the defendant wrongfully possessed and that rightfully belonged to the plaintiff.” The Fourth Circuit remanded the case to the district court to assess whether the plaintiff plausibly alleged such a claim.

What The Court Did Not Address

There are other requirements and limitations in ERISA Section 502(a)(3) that the Fourth Circuit’s *Rose* decision did not address. Perhaps most importantly, Section 502(a)(3) does not simply authorize a claim for “equitable relief”; it authorizes a claim for “other,” appropriate” equitable relief, and relief to remedy a breach of ERISA or a plan. The Supreme Court, and Fourth Circuit, have held that the phrase “other appropriate” creates a limitation on the relief available under Section 502(a)(3); so does the requirement that the relief must be appropriate in order to remedy a breach.

To determine whether relief sought is “other appropriate” under Section 502(a)(3), courts are supposed to consider, among other things, the entirety of Section 502(a) and the limits Congress purposely placed on the causes of action available under ERISA. As a general rule, monetary damages are available under Section 502(a)(2), and only against a fiduciary. The Fourth Circuit seemingly could have held that because monetary relief

under ERISA is limited, because it is available only against a fiduciary under 502(a)(2), Congress did not intend for 502(a)(3) to ignore that limitation and allow monetary relief against anyone. This is particularly true if the defendant is a fiduciary, as it was in *Rose*. The plaintiff in *Rose* sought equitable compensation and surcharge, which are remedies traditionally available in trust cases only against fiduciaries, and it would seem that because 502(a)(2) specifically addresses limit circumstances when a plaintiff can recover monetary relief against a fiduciary, 502(a)(3) should not be read to broaden those circumstances.

In addition, the Fourth Circuit did not address the requirement in 502(a)(3) that the relief sought must be appropriate to remedy a breach. Courts have held that this means that there must be some reasonable relation between the breach alleged and the relief sought, so that the relief is appropriate to remedy the alleged breach. It is unclear at what stage in litigation a court is supposed to address whether the relief sought is appropriate to remedy the particular breach. To give an example, imagine a plaintiff sued to recover an equitable remedy like "rectification," which is when a court orders changes to a document. If a plaintiff were to request that an ERISA plan be re-written to expressly state that benefits must be provided to that plaintiff, for her particular claim, that would be an equitable remedy. But it likely would not be an "appropriate" equitable remedy, because amending an entire plan to address one claim is not reasonable. Shouldn't a plaintiff also have the burden of pleading facts to plausibly show that the remedy sought is not only equitable, but also appropriate? This question is not answered in *Rose*.

Application To ESOP Cases

Relatively recently, plaintiffs in ESOP cases have been expanding the universe of defendants, typically by naming selling shareholders and seeking restitution or disgorgement of money the selling shareholders received in an ESOP transaction. Some pleadings have sought a variety of remedies that appear to be equitable, but, in actuality, are not. This includes surcharge. One of the fundamental questions courts have to address is what a plaintiff has to plead in order to state a claim for equitable relief. Some courts have not required plaintiffs to plead important aspects of common equitable remedies, such as a constructive trust or equitable lien that require a plaintiff to identify specific funds a defendant possesses that should be returned to a plaintiff. Other courts have not engaged in a thorough analysis to truly determine whether the relief sought was legal or equitable in nature, but have accepted labels without scrutiny.

Selling shareholders in ESOP transaction cases should be mindful of the complexity of a 502(a)(3) claim and the importance of analyzing whether a complaint pleads the basis to obtain equitable relief, and whether the relief sought actually is equitable. If not, then the complaint may be subject to dismissal.

In Summary

- In *Rose v. PSA Airlines, Inc.*, the Fourth Circuit held that ERISA Section 502(a)(3), which permits a claim for "other appropriate equitable relief," does not allow claims to recover money from a defendant's general assets.
- There are other requirements and limitations in ERISA Section 502(a)(3) that the *Rose* decision did not address including that Section 502(a)(3) does not simply authorize a claim for "equitable relief"; it authorizes a claim for "other," appropriate" equitable relief, and relief to remedy a breach of ERISA or a plan. ❂

Notes

1. Rose v. PSA Airlines, Inc., 80 F.4th 488 (4th Cir. 2023).
2. 29 U.S.C. § 1132(a)(3).

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