

Liability for Fiduciary Breach Not Dischargeable in Personal Bankruptcy

November 19, 2012

The Department of Labor (“DOL”) sued the president of several related companies to establish his personal liability for more than \$67,000 in employee contributions never remitted to the employer sponsored benefit plans and to prevent him from discharging this liability in his pending personal bankruptcy action. Over a nearly three-year period, the companies withheld but never remitted the employee contributions to the companies’ group health and 401(k) plans (the “Plans”). The court concluded that, under ERISA, the president was a “functional fiduciary” of the Plans because he exercised discretionary control over plan assets “the employee contributions” when he retained those funds in the companies’ general assets to pay other corporate debts, rather than timely remitting them to the Plans as required by ERISA. The president’s conduct also violated several other ERISA provisions, including the duty of loyalty, exclusive benefit rule, and prohibited transactions rule. Accordingly, he was personally liable for the unremitted employee contributions. The court further concluded that the president had committed “defalcation” while acting in a fiduciary capacity. Defalcation is something more than negligence or accident but less than fraud or embezzlement. Consequently, his liability was not dischargeable under bankruptcy law. In a related case, the DOL sought to recover a portion of the unremitted employee contributions from the directed trustee of one of the 401(k) plans. That court concluded that the trustee was personally liable for the ERISA violations of his co-fiduciary, the president, because the trustee failed to monitor or ensure that the employee contributions were timely remitted to the 401(k) plan. And like the president, the trustee committed defalcation while acting in a fiduciary capacity and could not discharge this liability in bankruptcy. *In re John Dombek III*, No. 11-40894 (Bankr. N.D. Ill. Oct. 16, 2012); *In re John Dombek Jr.*, No. 12-00564 (Bankr. N.D. Ill. Oct. 5, 2012).