

# Bloomberg Tax

## Supreme Court Decision Modifies ERISA Litigation Landscape

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The Supreme Court's unanimous [Cunningham v. Cornell](#) decision on excessive fee lawsuits under the [Employee Retirement Income Security Act of 1974](#) has significant implications for the plan sponsor community. The case has been widely characterized as a win for plaintiffs because the court lowered the standard for pleading a prohibited transaction claim under ERISA. Allowing more claims to survive a motion to dismiss, however, could subject defendants to costly and time-intensive discovery for ultimately meritless claims. This article briefly discusses the civil procedure tools the court listed to help defendants defeat meritless claims early on and suggests that defendants consider shifting their focus away from avoiding discovery entirely.

Justice Samuel Alito, [concurring](#) with the majority's statutory interpretation, raised concerns about the decision's real-world consequences, warning that the holding would cause "untoward practical results" and urging lower courts to strongly consider using the court's proposed "alternative safeguards."

Those safeguards include challenging standing, using [Federal Rules of Civil Procedure](#) 7 and 11, leaning on ERISA's fee-shifting provision, and asking judges to limit discovery. Unfortunately, each of these tools is generally untested, rarely employed by courts, and/or difficult to use effectively prior to discovery. Although the court's endorsement may help these tools gain more traction, they are not obviously calculated to hand defendants an early dismissal of meritless prohibited transaction claims.

### Standing Challenges Offer Potential, But May Not Avoid Discovery

The court pointed out that complaints that do not "plausibly and clearly allege a concrete injury" could be dismissed for failing to satisfy Article III's constitutional standing requirements. Defendants may move to dismiss such claims for lack of subject matter jurisdiction under Rule 12(b)(1). Standing challenges are not unusual in ERISA class actions, and the Supreme Court affirmed such a dismissal in [Thole v. U.S. Bank, N.A.](#)

Though standing challenges can be effective in ERISA class action litigation, they rarely completely eliminate the need for discovery. Courts may be slow to rule, or otherwise permit some limited discovery before ruling. In [Thole](#), the district court denied an initial Rule 12(b)(1) motion, and the parties engaged in a year of discovery before a

renewed motion was granted. Accordingly, even an ultimately successful standing challenge may not avoid all discovery.

## **Rule 7(a)(7) Provides an Untested Avenue for Dismissal**

The court also pointed to the rarely used Rule 7(a)(7), which “empowers” district courts to require plaintiffs to reply to an answer where the defendant has asserted facts establishing a prohibited transaction exemption. Alito’s concurrence, joined by Justices Clarence Thomas and Brett Kavanaugh, identified Rule 7 as the “most promising” post-*Cunningham* tactic.

Yet the mechanism remains largely untested—particularly in ERISA litigation. And in the few reported instances when the rule has been used, the results have been mixed. For example, in one 2013 case, a malicious prosecution claim was [dismissed](#) after the plaintiff could not rebut a governmental immunity defense raised in the answer. But in a similar 2022 case, a district court [declined](#) to dismiss, illustrating the uncertain nature of this strategy. Until this tactic has been tested in ERISA cases, its effectiveness remains speculative.

## **Rule 11 Sanctions and ERISA Fee Shifting Are Uncommon Remedies**

The court’s opinion pointed to possible Rule 11 sanctions in cases where “an exemption obviously applies, and a plaintiff and his counsel lack a good-faith basis to believe otherwise.” But judges, who value zealous advocacy, rarely impose Rule 11 sanctions. One study [found](#) that 91% of judges do not believe sanctions should be mandatory even when a violation is found.

For Rule 11 sanctions to even be on the table, defendants must first [make a showing](#) that the plaintiff failed to conduct a reasonable inquiry into the law and facts before filing a complaint, or do not have a good faith basis to continue to pursue their claims. This could require defendants to produce evidence demonstrating the applicability of an exemption. In some cases, discussions with plaintiffs about whether an exemption is satisfied may not be effective unless defendants are willing to voluntarily share operational information, something defendants are often hesitant to do.

Similarly, although ERISA includes a fee-shifting provision that allows prevailing parties to recover attorneys’ fees, courts have adopted varying standards for when fee awards are appropriate, many of which are unfavorable to defendants. The uncertainty surrounding this provision further limits its effectiveness as a deterrent.

## **Shifting Focus to Limiting Discovery**

Although the tools highlighted by the Supreme Court seek to offer relief at the pleading stage through early dismissal, its strong support for narrowing discovery may prove more impactful. The Court encouraged district courts to use their “discretionary authority to expedite or limit discovery” to prevent unnecessarily high litigation costs.

Historically, persuading courts to significantly limit discovery in ERISA class actions has been difficult—largely due to the asymmetry of information in such cases. Notwithstanding ERISA’s statutory disclosure requirements, courts view plaintiffs as lacking access to key documents and data that reside with plan fiduciaries and are hesitant to deny them the chance to access that information through discovery. However, the court’s endorsement of district courts limiting expansive discovery may help defendants place limits on early discovery. For example, courts may be more open to a phased approach to discovery that prioritizes determining whether there is a valid exemption defense to a prohibited transaction claim before allowing broad discovery. Defendants could use such phased discovery to support early summary judgment motions to bring a quicker end to meritless prohibited transaction claims. So, although the *Cunningham* decision’s suggested approaches to avoiding discovery may have limited practical use, it may nevertheless help reduce the heavy discovery burdens ERISA class actions place on defendants.

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