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CLIENT ALERT

Notes vs. Certificates: Second Circuit Draws Critical Distinction in ERISA Plan Asset Case

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In its recent ruling in *Powell v. Ocwen Financial Corporation*, the Second Circuit addressed whether certain residential mortgage-backed securities ("RMBSs") and their underlying mortgages constituted plan assets subject to the fiduciary protections of ERISA.[1] The court affirmed summary judgment for defendants relating to indenture notes, holding that the notes and their underlying mortgages did not qualify as plan assets.[2] The court also reversed summary judgment as to real estate investment mortgage conduit ("REMIC") trust certificates.[3] It concluded the certificates represented beneficial interests in the issuing trusts and triggered the Department of Labor's ("DOL") look-through exception and were thus plan assets.[4] The *Powell* decision is noteworthy for its careful application of the DOL's plan-asset regulation to large defined benefit pension plans and its implications for investment providers.

1 The Employee Retirement Income Security Act of 1974, as amended; *See Powell as Tr. of United Food & Com. Workers Union & Emps. Midwest Pension Fund v. Ocwen Fin. Corp.*, No. 23-999, 2026 WL 828159 (2d Cir. Mar. 26, 2026).

2 *Powell*, 2026 WL 828159, at *10.

3 *Id.*

4 *Id.* at *8–9.

The District Court Held the RMBSs and REMICs Did Not Hold Plan Assets

Trustees of the United Food & Commercial Workers Union & Employers Midwest Pension Fund (the "Plan"), a defined benefit pension plan regulated under ERISA, invested the plan's funds in classes of RMBSs issued by trusts.[5] The trusts included Delaware statutory trusts that issued notes pursuant to indenture agreements and other trusts governed by New York law and classified as REMICs for tax purposes that issued regular interest certificates.[6]

Each trust appointed a master servicer to oversee the collection of payments on the underlying mortgages.[7] Wells Fargo Bank, N.A. ("Wells Fargo") served as master servicer for some of the trusts, while Ocwen was assigned the right to service the mortgages underlying all the trusts.[8] In 2018, the trustees filed a putative class action in the Southern District of New York alleging that Ocwen breached fiduciary duties under ERISA by mismanaging the mortgages and engaging in prohibited transactions, and that Wells Fargo breached its co-fiduciary and oversight duties.[9]

The defendants moved to dismiss for, among other reasons, failure to state a claim.[10] They argued the underlying mortgages were not plan assets under ERISA and that "Ocwen did not act in a fiduciary capacity vis-à-vis the Plan."[11] The district court converted the motions into summary judgment motions and directed the parties to conduct limited discovery on the plan-asset and fiduciary-status questions.[12] Following discovery, the parties cross-moved for summary judgment.[13] The district court granted defendants' motion and denied the trustees' cross-motion, holding that both the indenture notes and the regular-interest certificates were "treated as indebtedness under applicable local law" and had "no substantial equity features," and therefore the look-through exception did not apply to any of the Plan's investments.[14] The district court entered judgment for all defendants, and the trustees appealed.[15]

Defining Plan Assets

ERISA imposes fiduciary duties on those who manage or control plan assets, but the statute does not define what constitutes a plan asset.[16] Congress delegated that task to the DOL, which implemented a plan-asset regulation providing the general rule that "when a plan invests in another entity, the plan's assets include its investment, but

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5 *Id.* at *2.
6 *Id.*
7 *Id.* at *3.
8 *Id.*
9 *Id.* at *3–4.
10 *Id.* at *4.
11 *Id.*
12 *Id.*
13 Id.
14 *Id.*
15 *Id.*
16 Final Regulation Relating to the Definition of Plan Assets, 51 Fed. Reg. 41,262, 41,263 (Dep't of Labor Nov. 13, 1986).

do not, solely by reason of such investment, include the underlying assets of the entity."[17] There is, however, a critical look-through exception: when a plan invests in an equity interest of an entity that is "neither a publicly-offered security nor a security issued by an investment company registered under the Investment Company Act of 1940," the plan's assets include an undivided interest in each of the underlying assets of the entity and the equity interest.[18] Whether an investment is an equity interest turns on two inquiries: first, whether the instrument "is treated as indebtedness under applicable local law," and second, whether it "has no substantial equity features."[19] If the answer to either question is in the negative, the investment qualifies as an equity interest.[20] The regulation further provides that certain interests such as "[a] profits interest in a partnership, an undivided ownership interest in property[, or] a beneficial interest in a trust are equity interests."[21] In *Powell*, the Second Circuit applied this framework, reaching different conclusions for the indenture notes and the REMIC trust certificates.

Second Circuit Distinguishes Debt-Structured Indenture Notes from Equity-Based REMIC Certificates

The Second Circuit affirmed the district court's holding that the Plan's investments in indenture trusts that issued notes were debt instruments without substantial equity features under the DOL's plan-asset regulation, and therefore the underlying mortgages were not plan assets. The Second Circuit reached a different conclusion than the district court regarding the Plan's investments in the REMIC trusts, which took the form of regular-interest certificates.[22] The court agreed with the trustees that the certificates represented "beneficial interests in a trust" which the DOL's regulation expressly defines as equity interests.[23]

The court concluded the indenture trust notes looked like traditional debt because they promised interest and payments on a fixed schedule and the plan did not own any of the underlying mortgages.[24] Although the DOL's regulation does not define substantial equity features, the DOL has observed that whether an investment has equity features is "an inherently factual question" and that a debt instrument with "some equity features does not require characterization of the instrument as an equity interest."[25]

The court came to the determination that the notes reflected a traditional debt structure because each trust issued note entitled "noteholders to receive fixed payments of interest and principal at regular intervals [with] fixed maturity dates."[26] The Second Circuit also reasoned that the trustees' focus on the subordination of the notes, finance of the mortgage pool, and thin capitalization were not enough to find the notes had substantial equity features because none of the features highlighted by the court created residual interests in the trusts or their estates as required

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17 Definition of "plan assets" – plan investments, 29 C.F.R. § 2510.3-101(a)(1)–(2).

18 *Id.* at § 2510.3-101(a)(2).

19 *Id.* at § 2510.3-101(b)(1).

20 *Id.* at § 2510.3-101(a)(2).

21 *Id.* at § 2510.3-101(b)(1); 51 Fed. Reg. 41,265, *Powell*, 2026 WL 828159 at *5-7.

22 *Id.* at *8.

23 *Id.*

24 *Id.* at *6.

25 Final Regulation Relating to the Definition of Plan Assets, 51 Fed. Reg. 41,265-66, (Dep't of Labor Nov. 13, 1986).

26 *Powell*, 2026 WL 828159 at *6.

under a traditional equity framework.[27] The court was also unmoved by the trustees' argument that repayment of the notes was dependent on the performance and value of the underlying mortgages, calling these circumstances a "[u]niversal credit risk" that "is not – and cannot be a substantial *equity* feature."[28]

The court also declined to apply the Ninth Circuit's functional two-part test from *Kayes v. Pacific Lumber Co*., which would have asked whether the plan's underlying assets could be used to benefit the fiduciary at the expense of plan participants to determine plan assets.[29] The court reasoned that Congress delegated authority to the DOL to define plan assets, and the DOL's controlling regulation governed the analysis.[30] Further, the trustees did not challenge the validity of the DOL's regulation, and thus the court's analysis "beg[an] and end[ed] with the plan-asset regulation."[31]

In comparison to the notes, the REMIC trusts separately issued certificates representing residual interests that were subordinated to the notes.[32] Under New York law, which governed each REMIC trust, a beneficial interest in a trust encompasses "[a]ny right given by the trust instrument to receive a benefit from the trust in some contingency."[33] The court examined the governing trust agreements and found that holders of the regular-interest certificates were identified as beneficiaries of the trusts.[34] For example, a depositor conveyed "the underlying mortgage pool" to the Trustee to create a trust for the benefit of the certificate holders of one of the trusts.[35] The trust agreement required the trustee to collect payments on the underlying mortgages and deposit proceeds into accounts maintained "for the benefit of the Certificateholders . . . in trust."[36] The trustee then paid regular-interest certificate holders their share of the proceeds.[37] The governing documents for the three certificate issuing trusts had similar provisions.[38]

The Second Circuit rejected Ocwen's and Wells Fargo's claim that only holders of residual certificates were trust beneficiaries.[39] The court further observed that its conclusion aligned with the plan regulations' specific exception for guaranteed governmental mortgage pool certificates.[40]

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27 *Id.* at *5.

28 *Id.* at *7.

29 *Id.*

30 *Id.*; 29 U.S.C. § 1002(42).

31 *Powell*, 2026 WL 828159 at *7.

32 *Id.* at *6.

33 *Schoellkopf v. Marine Tr. Co. of Buffalo*, 267 N.Y. 358, 362 (N.Y,1935); see also N.Y. Est. Powers & Trusts Law § 11-A-1.2(2), (5) (McKinney 2002).

34 *Powell*, 2026 WL 828159 at *8.

35 *Id.*

36 *Id.*

37 *Id.*

38 *Id.*

39 *Id.*at *9.

40 *Id.*; Definition of "plan assets" – plan investments, 29 C.F.R. § 2510.3-101(i)(1).

Ocwen's Fiduciary Status

The defendants further argued that even if the mortgages underlying the REMIC trusts were plan assets, Ocwen's servicing of those mortgages did not constitute a fiduciary function under ERISA.[41] The case was remanded for further proceedings on that issue given the district court had not addressed it.[42]

Key Takeaways

The Second Circuit's decision in *Powell* has important implications for ERISA litigants. The threshold question of whether an investment qualifies as an equity interest under the DOL's plan-asset regulation must be carefully analyzed at the start of the case. Despite defined benefit pension plans being sophisticated investors, they remain entitled to ERISA's fiduciary protections for plan assets. This is reflected in both the district court's analysis and the Second Circuit's careful application of the DOL's plan-asset regulation six underlying investment instruments. Plaintiffs seeking to extend fiduciary liability to underlying assets will look for equity characteristics under ERISA's plan asset rules.

Powell also shows that courts will ground their analysis in the governing regulatory framework. Although courts have recently shown less deference to agencies following *Loper Bright Enterprises v. Raimondo*, here the Second Circuit cited *Loper Bright* only to point to the DOL's plan-asset regulation. This is a benefit for potential defendants and fiduciaries given the DOL has provided more specific guidance regarding whether a particular investment vehicle holds plan assets. At the same time, the case illustrates that some courts may not decide fiduciary status at the motion to dismiss stage because they prefer to have discovery first.

We will continue to closely monitor these legal developments in the ERISA space.

41 *Powell*, 2026 WL 828159 at *9.

42 *Id.*

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work. [43]

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