

Publications

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North Carolina Federal Court Lets ESOP Fiduciary Claims Proceed, Underscoring Active Oversight Duties

Key Takeaways

- A North Carolina district court largely denied motions to dismiss ERISA and malpractice claims arising from a leveraged ESOP transaction and subsequent sale, allowing fiduciary breach claims against an independent trustee, private equity investors and transaction counsel to proceed.
- The court emphasized that ESOP trustees must actively investigate red flags and advocate for plan participants, rejecting arguments that a trustee may simply rely on process formalities.
- Although this litigation remains in the early stages, the court's refusal to dismiss most ERISA fiduciary claims reinforces the judiciary's expectation that ESOP fiduciaries must actively safeguard participant interests.

The U.S. District Court for the Western District of North Carolina denied on March 3 motions to dismiss ERISA-related claims involving the employee stock ownership plan (ESOP) of Hollandia Produce Group Inc.

The plaintiffs — former employees of Hollandia Produce Group Inc. — allege that the ESOP's value was improperly diminished in connection with a transaction financed by private equity investors and later sold for \$122.5 million in 2022. Despite the ESOP's alleged 100% ownership of the company, the complaint asserts the ESOP received less than \$3.1 million from the sale.

While the court dismissed two claims — a malpractice claim against the trustee and a prohibited transaction claim tied to the ESOP's 2015 formation — both as time-barred under ERISA's six-year statute of repose, many ERISA fiduciary claims survived the motion to dismiss.

Court's Analysis: Fiduciary Duties Cannot Be Passive

A central theme in the court's ruling is that a fiduciary's obligations under ERISA cannot be passive.

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The trustee argued that it was not required to serve as a “white knight” to uncover the allegedly fraudulent scheme. The court rejected this view, stating that an ERISA fiduciary has a duty to prudently manage plan investments and may be held liable for failing to investigate red flags.

The court further explained that a trustee is not permitted to “sit back, go through the motions and collect checks.” Rather, the trustee must advocate for plan beneficiaries and ensure plan assets are maximized for their benefit.

Implications for ESOP Transactions and Private Equity Sponsors

Although this ruling is in the early stages and addresses pleading-stage standards, it highlights several recurring ERISA-related issues in ESOP transactions:

1. **Heightened Scrutiny of Independent Trustees.** Courts continue to emphasize that trustees must independently evaluate transaction structure and post-closing governance.
2. **Risk Exposure for Investors and Directors.** The decision allows claims against private equity funds to proceed past the pleading stage, reinforcing that investor involvement in ESOP transactions may invite fiduciary scrutiny depending on alleged conduct.
3. **Counsel’s Role in Transaction Structuring.** Claims against transaction counsel also proceeded past the pleading stage, indicating that advisory roles in ESOP transactions are becoming subject to a more fact-intensive review.

Practical Implications for ESOP Fiduciaries, Sponsors and Advisors

While the *Hollandia Produce* litigation remains in its early stages, the court’s refusal to dismiss most of the ERISA fiduciary claims reinforces the judiciary’s expectation that ESOP fiduciaries must actively safeguard participant interests.

For sponsors, trustees and advisors involved in ESOP transactions, proactive governance and careful documentation remain critical to mitigating litigation exposure.

The Polsinelli ESOP Group advises sponsors, trustees and portfolio companies on structuring, governance and exit considerations in ESOP transactions. If you would like to discuss how this ruling may affect your organization, please contact your regular Polsinelli attorney or a member of the Polsinelli ESOP Group.