Legal Developments in Fiduciary Cases

This week has been a busy week for plan fiduciary cases. First, the Eighth Circuit issued its widely anticipated excessive fee decision in Tussey vs. ABB. Next, the Supreme Court signaled it may be interested in deciding whether 401(k) plan fiduciaries can be in breach of their duties over investment choices. Lastly, the Supreme Court will hear arguments on April 2 in another fiduciary case, Fifth Third Bancorp et al. vs. Dudenhoeffer, which could make it easier for participants to challenge employers when company stock loses value.

Based on these cases, as suggested by the articles below, plan fiduciaries and service providers should ensure their plan document and summary plan description impart deference to decisions made regarding the plan; implement best practices with respect to the monitoring and disclosure of revenue sharing fees paid to plan service providers; monitor the decisions of investment manager, consultants and other service providers; and create records that illustrate plan fiduciaries' decision-making process and their considerations.

Source: Practical Law

Eighth Circuit Issues Widely Anticipated Excessive Fee Decision in Tussey v. ABB

In *Tussey v. ABB, Inc.*, the US Court of Appeals for the Eighth Circuit upheld, vacated and remanded, and reversed in part a decision from the District Court for the Western District of Missouri regarding breach of fiduciary duty claims for excessive recordkeeping fees and the imprudent selection of plan investment funds.

Practical Law Employee Benefits & Executive Compensation

A panel of the US Court of Appeals for the Eighth Circuit rendered a much anticipated decision in *Tussey v. ABB*, which is one of the first excessive fee class action lawsuits to go to trial on almost all of the pleaded claims (*No. 12–2056, 2014 WL 1044831 (8th Cir. Mar. 19, 2014)*). The Eighth Circuit affirmed in part, vacated in part, reversed in part and remanded the district court's decision.

Background

Defendant ABB sponsored two 401(k) plans for its employees. A committee of ABB individuals oversaw all of ABB's employee benefit programs and was the named plan administrator of the plans. Fidelity was a recordkeeper and service provider to the plans. Beginning in 2001, the plans offered Fidelity target-date funds (Fidelity funds) as plan investment options and monies that were invested in a Vanguard balanced fund (Vanguard fund) were mapped to the Fidelity funds, unless affected participants chose to invest those monies in other plan investment options.

Defendant Fidelity Trust acted as the recordkeeper for the plans. Over time, Fidelity Trust was primarily paid through a revenue-sharing arrangement by which Fidelity Trust was paid a percentage of the plans' assets from participants' accounts in a particular fund. Revenue-sharing came from some of the investment companies whose products were selected by ABB for the plans. These investment companies gave Fidelity Trust a percentage of the income they received from plan participants who selected their company's investment options.

The plaintiffs brought claims on behalf of a class of present and former ABB employees who are participants in the plans. The district court held that several ABB and Fidelity defendants, including ABB, the plan's committee, Fidelity Research and Fidelity Trust, breached their ERISA fiduciary duties to the plans by:

- Failing to monitor and control recordkeeping fees.
- Paying excessive revenue-sharing fees from plan assets to subsidize other corporate services.
- Mapping (transferring) funds held in the Vanguard fund to the Fidelity funds, in violation of the plan's Investment Policy Statement (IPS).
- Selecting more expensive share classes when less

expensive share classes were available.
- Not distributing float income solely in the plans' interest.

The district court awarded a $36.9 million judgment against ABB Inc. and Fidelity Management & Research Co., including $13.4 million for the recordkeeping claim, $21.8 million on the investment and mapping claims and $1.7 million based on float income. The defendants appealed the district court's decision to the Eighth Circuit.

Outcome

The Eighth Circuit upheld the $13.4 million decision against ABB regarding recordkeeping fees paid to Fidelity, but reversed and remanded the $21.8 million award based on losses due to mapping from the Vanguard fund to Fidelity's funds. The Eighth Circuit also reversed the $1.7 million based on float income.

Ultimately, the Eighth Circuit:

- Found that the district court should have applied an abuse of discretion standard of review (*Firestone*deference) to the plan fiduciaries' decisions, rather than a *de novo* standard (see *Applying Firestone Deference to Fiduciary Breach Claims*).
- Affirmed the district court's holding that the ABB fiduciaries breached their fiduciary duty to the plans on the recordkeeping issue (see *Recordkeeping*).
- Vacated the district court's holding that the defendants improperly selected and mapped plan investments and remanded the case to the district court to apply *Firestone* deference to the mapping claims and redetermine damages (see *Selection and Mapping of Investment Options*).
- Reversed the district court's holding that the defendants breached their fiduciary duty of loyalty by improperly using float income (see *Float*).

Applying Firestone Deference to Fiduciary Breach Claims

The defendants argued that an abuse of discretion standard should be applied to the plan fiduciaries' decisions because the plan gave the plan administrator broad discretion to interpret and apply the terms of the plan, commonly known as *Firestone* deference (see *Standard Clauses, Plan Language, Firestone Plan Interpretation* and *SPD Language, Firestone Plan Interpretation*). However, the district court agreed with the plaintiffs that this discretion is limited to the plan administrator's determination of benefit claims and does not extend to breach of fiduciary duty claims or claims regarding its interpretation of the IPS. Therefore, the district court applied a *de novo* standard of review to the plaintiffs' claims.

The Eighth Circuit did not rule on whether the IPS is a plan document, the interpretation of which may be subject to *Firestone* deference separately from the breach of fiduciary duty claims. However, it did apply the more deferential abuse of discretion standard to the breach of fiduciary duty claims, noting that it follows most circuits in not limiting *Firestone* deference to benefits claims (see *Legal Update, Ninth Circuit Joins Circuit Splits in ERISA Section 404(c) Opinion and Defers to DOL Interpretation of Safe Harbor*).

The issue of whether to apply *Firestone* deference to fiduciary breach claims is a contested issue. The US Court of Appeals for the Ninth Circuit recently held in *Tibble v. Edison Int'l* that the *Firestone* standard of review applies to ERISA fiduciary duty and conflict of interest cases and not just benefit claims (see *Legal Update, Ninth Circuit Joins Circuit Splits in ERISA Section 404(c) Opinion and Defers to DOL Interpretation of Safe Harbor*). *Tibble* has been appealed to the US Supreme Court and, after the case went to conference on March 21, 2014, the Supreme Court requested input from the Solicitor General.

Recordkeeping

The district court found that the ABB fiduciaries breached their fiduciary duty to the plans by failing to properly calculate and monitor the plans' recordkeeping costs and by paying excessive revenue-sharing fees (see *Legal Update, Failure to Monitor Recordkeeping Fees is a Breach of Fiduciary Duty under ERISA: Missouri District Court: Failing to Monitor Recordkeeping Costs and Negotiate Rebates*).

The ABB fiduciaries raised several issues on appeal that challenged the district court's holding on the recordkeeping issues. The court rejected these arguments, reasoning:

- A claim of unreasonable recordkeeping fees is not barred solely because a 401(k) plan offers a wide range of investment options from which participants may choose, particularly when, as in this case, the facts involve allegations of wrongdoing with respect to fees.
- The district court's factual findings on the recordkeeping issues are well-supported by the record and its legal conclusion was not erroneous. This is an important point as it validates the district court's legal findings that the ABB fiduciaries failed to:
  - calculate the amount the plan was paying Fidelity for recordkeeping through revenue sharing;
  - determine whether Fidelity's pricing was competitive;
  - adequately leverage the plan's size to reduce fees; and
  - make a good faith effort to prevent the subsidization of administration costs of ABB corporate services with plan assets, even after ABB was notified by plan counsel that the plan was overpaying for recordkeeping fees.
- The district court did not abuse its discretion in awarding $13.4 million as damages based on the expert's testimony because:

- the district court has considerable discretion in determining the reliability of the expert's testimony;
- the district court ruled on the expert's reliability when it denied the fiduciaries' challenge before trial; and
- the fiduciaries cross-examined the expert at trial.

Selection and Mapping of Investment Options

The district court found that the selection of the Fidelity funds as investment options for the plans and the decision to map plan investments from the Vanguard fund to the Fidelity funds was imprudent and improperly influenced by conflicts of interest (see *Legal Update, Failure to Monitor Recordkeeping Fees is a Breach of Fiduciary Duty under ERISA: Missouri District Court: Selection and De-selection of Investments*).

In its appeal to the Eighth Circuit, the ABB fiduciaries challenged the timeliness of the plaintiffs' claim, the district court's interpretation of the plan and the IPS, and the basis for determining damages.

The Eighth Circuit held that the plaintiffs' mapping claim is not time-barred, but it vacated the district court's judgment and award on this claim and remanded for further consideration, because:

- The district court did not properly apply ERISA's prudent person standard when evaluating the fiduciaries' investment decisions because it was influenced by hindsight, evidenced by its comparison of the eventual better performance of the Vanguard fund to the Fidelity funds. Under the prudent person standard, a fiduciary has discretion to choose plan investments to the extent its investment choices are reasonable in light of what it knows at the time (see *Practice Note, ERISA Fiduciary Duties Duty of Prudence*).

- The district court's failure to apply *Firestone* deference to the ABB fiduciaries' evaluation and selection of plan investments was erroneous and may have affected the court's decision in this matter.

The Eighth Circuit also ruled that the district court should reevaluate its method of calculating the damage award on the investment selection and mapping claims. The district court determined the plan participants' mapping damages based on the amount that participants would have made had their monies been continuously invested in the Vanguard fund. According to the Eighth Circuit, a more reasonable way of measuring participants' mapping damages would be to compare the difference between:

- The performance of the Fidelity funds.
- The minimum return of the subset of managed allocation funds the ABB fiduciaries could have chosen without breaching their fiduciary duties.

The Eighth Circuit also held that the district court incorrectly inferred that the participants who invested in the Fidelity funds would have invested (and remain invested) in the Vanguard fund if it had not been removed from the plan. Therefore, the district court's $21.8 million award of damages is speculative and may exceed the losses to the plan resulting from the breach.

Float

The district court found that the improper use of float income by Fidelity was a breach of Fidelity's fiduciary duty of loyalty because it transferred float income to the underlying investment options, rather than to the plans. For these breaches, the court found Fidelity liable for $1.7 million in losses suffered by the plans (see *Legal Update, Failure to Monitor Recordkeeping Fees is a Breach of Fiduciary Duty under ERISA: Missouri District Court: Float*).

The Eighth Circuit reversed the district court's judgment against Fidelity, agreeing with Fidelity that the investment options, and not the plan:

- Held property rights in the float.
- Bore the risk of loss on the float accounts.
- Were entitled to the benefits of ownership (float income).

In contrast, the Eighth Circuit found that the plan had no property rights in the float because:

- Both float accounts, the depository account and the redemption account were registered for the benefit of the plan's investment options.
- Once the plan became owner of shares of a mutual fund, it was no longer the owner of the money used to purchase them, which flowed to the investment options through the depository account. The plan investment options held the property rights in the depository float and were entitled to float income. The court reasoned that when a plan participant chooses to receive a check rather than an electronic disbursement:
    - the plan investment options retains all rights to the redemption float (held in the redemption account) until the disbursement check is cashed; and
    - the plan has no ownership rights to float income from the redemption account.

Fidelity clearly won on the float issue in this case, but employers should be aware that:

- The Department of Labor (DOL) issued Field Assistance Bulletin 2002-03, which requires fiduciaries of plans whose service providers retain float in the same bank account as plan assets to evaluate the service providers' float handling procedures and the

compensation they are paid from it when negotiating a reasonable fee arrangement (see *Practice Note, Negotiating Service Provider Agreements: Special Fee Issues: Float*).
- Judge Bye of the Eighth Circuit filed a dissenting opinion on this issue, arguing that he was persuaded by the ERISA regulations and DOL authority that float was in fact a plan asset, and that he would have found that Fidelity breached its duties.

Attorneys' Fees

The Eighth Circuit vacated the district court's award for attorneys' fees because it vacated the court's mapping award and reversed the judgment against Fidelity. The district court will have to determine the reduction in attorneys' fees when it resolves the remaining issues on remand.

Practical Implications

There are several practical implications that employers, plan fiduciaries and service providers should consider as a result of this decision, including:

- The importance of including broad *Firestone* language in the plan document and SPD imparting deference to decisions made regarding the plan (for sample language, see *Standard Clauses, Plan Language, Firestone Plan Interpretation* and *SPD Language, Firestone Plan Interpretation*).
- Best practices with respect to the monitoring and disclosure of revenue sharing fees paid to plan service providers (see *Practice Note, Service Provider Disclosure Requirements for Pension Plans: Disclosure of Recordkeeping Services Paid Through Revenue-sharing*). Plan fiduciaries should consider adopting the following practices that are based on the district court's findings in this case:
  - calculating the amount the plan is paying for

recordkeeping through revenue-sharing (this coincides with the requirement under ERISA Section 408(b)(2) regulations that the service provider provide a plan that utilizes revenue-sharing with a good faith estimate of the cost of recordkeeping services);
    - determining whether the recordkeeper's pricing is competitive;
    - leveraging the plan's size to reduce fees (for larger plans);
    - making a good faith effort to prevent the subsidization of costs for other services with plan assets; and
    - taking and documenting action if advised by counsel that recordkeeping fees are potentially excessive.
- Having in place and following procedures to monitor the decisions of investment managers, consultants and other service providers (see *Practice Notes, Negotiating ERISA Service Provider Agreements* and *Selecting and Hiring an Investment Manager*).
- Creating a record that illustrates the plan fiduciaries' decision-making process and their consideration of plan investment options to be added, removed or mapped to different options (see *Suggested Agenda Items for Plan Investment and Administration Committee Meetings Checklist*).
- Considering that Fidelity's victory on the float issue does not necessarily render the DOL's guidance on float inapplicable, which may still require a plan fiduciary to take float into consideration when negotiating a service provider's fee arrangement (see *Practice Note, Negotiating Service Provider Agreements: Special Fee Issues: Float*).

Source: pionline.com

Supreme Court signals interest in 401(k) plan fiduciary case

BY HAZEL BRADFORD | MARCH 24, 2014

The U.S. Supreme Court signaled its interest in deciding whether 401(k) plan fiduciaries can be in breach of their duties over investment choices.

The justices asked lawyers for the Labor Department and Justice Department to weigh in on Glenn Tibble et al. vs. Edison International et al. That request, announced Monday, is considered a strong indicator that the high court will take the case.

“This certainly increases the chances that the Supreme Court will hear this case,” said Thomas E. Clark Jr., chief compliance officer at FRA/PlanTools, a fiduciary consulting firm in Charlotte, N.C.

In March 2013, the 9th U.S. Circuit Court of Appeals in Pasadena, Calif., found that Edison International breached its fiduciary responsibilities by selecting retail-class shares in an investment fund, instead of lower-cost institutional-class shares. The case also raises other fiduciary issues, including statutes of limitations for filing such lawsuits and investment safe harbors.

Calls to Edison International were not returned at press time. As of Dec. 31, 2012, the Edison 401(k) Savings Plan, Rosemead, Calif., had $3.97 billion in assets.

On April 2, the Supreme Court will hear arguments in another fiduciary duty case, Fifth Third Bancorp, et al. vs. Dudenhoeffer, that could make it easier for participants to challenge employers when company stock loses value.

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Torrillo & Associates, LLC specializes in employee benefit plan audits including 401k audits, 403b audits, pension plan audits, and other retirement plan audits. We are licensed in 10 states including Pennsylvania, New Jersey, Delaware, New York and Florida. We are also able to practice in additional states that have passed firm mobility.

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