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## **COURT REVIEW 2009**

### **ERISA Plan Fees Litigation Rises to Take Appellate Spotlight in 2009**

After garnering much attention in the past couple of years at the trial court level, in 2009 the tax code Section 401(k) plan fees cases took the spotlight at the appellate level where three federal appeals courts tackled the often-controversial issues raised by the cases.

The plan fees cases came to the forefront of Employee Retirement Income Security Act litigation in 2006 after a small law firm in St. Louis filed a number of class action complaints against major companies that sponsored Section 401(k) plans. Other plaintiffs' firms later joined the fray and brought similar lawsuits.

In 2007 and 2008, the cases picked up steam and began to wind their way through the federal trial courts with a significant concentration of the cases in federal courts in Illinois. The cases met varying fates at the trial court level. Some of the cases were tossed on motions to dismiss or motions for summary judgment, while other cases were able to move beyond these motions and proceed to the class certification stage. To date, however, no case has been decided on its merits.

In 2009, three federal appeals courts were presented with some of the more high-profile plan fees cases. The U.S. Courts of Appeals for the Second, Seventh, and Eighth Circuits all confronted the cases and reached very different conclusions in the cases. For other cases still at the trial court level, there was a strong division among the federal district courts in many of the plan fees cases.

But while there was an uptick in the number of plan fees decisions in 2009, it appears that no new plan fees lawsuits were filed during the year.

#### **The Seventh Circuit and *Deere***

Early in 2009, the U.S. Court of Appeals for the Seventh Circuit became the first federal appeals court to tackle a Section 401(k) plan fee case. The Seventh Circuit ruled that a federal district court properly dismissed all fiduciary breach claims brought against the heavy equipment manufacturer Deere & Co. and its investment manager (*Hecker v. Deere & Co.*, 556 F.3d 575, 45 EBC 2761 (7th Cir. 2009)(28 PBD, 2/13/09; 36 BPR 357, 2/17/09)).

The lawsuit against Deere was filed by three employees who alleged that Deere breached its ERISA fiduciary duties by providing investment options in Deere's Section 401(k) plans that had excessive and unreasonable fees and costs. The employees also alleged that Deere and the plan's investment adviser, Fidelity Management Trust Co., violated ERISA by failing adequately to disclose information about the fees and costs to plan participants, such as revenue-sharing payments received by Fidelity.

The employees' lawsuit was dismissed by a federal district court in June 2007 before the employees had the opportunity to conduct discovery (121 PBD, 6/25/07; 34 BPR 1548, 6/26/07).

The case was then appealed to the Seventh Circuit, where the Deere employees and the Secretary of Labor argued that the appeals court should overturn the district court's dismissal of the lawsuit (58 PBD, 3/26/08; 35 BPR 726, 4/1/08). The ERISA Industry Committee, the National Association of Manufacturers, and the American Benefits Council filed briefs asking the Seventh Circuit to affirm the dismissal of the case ( 92 PBD, 5/13/08; 35 BPR 1133, 5/20/08).

#### **Major Points of *Deere* Ruling**

In its much-anticipated decision, the Seventh Circuit upheld the district court's dismissal of the lawsuit. Some of the key points of the Seventh Circuit's ruling include:

- Deere and the Fidelity companies had no duty to disclose the revenue-sharing arrangement that existed between Fidelity Trust and its affiliated company, Fidelity Management and Research Co. The court said revenue-sharing arrangements do not violate ERISA.
- Deere's disclosure of the total fees being paid to the investment funds, along with Deere's act of directing participants to the fund prospectuses for information about fund-level expenses, was "enough" to satisfy Deere's ERISA disclosure requirements.
- The Deere plans offered a sufficient mix of investments for their participants and thus even if some of the options charged excessive fees, no "reasonable trier of fact could find" that Deere failed to satisfy its

duty of providing a wide array of investment choices.

- The court said there was a wide range of expense ratios among the 20 Fidelity mutual funds offered under the plan and the 2,500 other funds available to plan participants through BrokerageLink. All of the funds were also offered to investors in the general public for the same expense ratio. The court added that nothing in ERISA would have required the plan fiduciaries to “scour the market to find and offer the cheapest possible fund.”
- The court refused to issue a specific ruling on whether ERISA Section 404(c)'s safe harbor applies to the selection of investment options for the plan, but the court ultimately said the safe harbor provision will protect a fiduciary that “satisfies the criteria” of Section 404(c) by including a sufficient range of investment options in the plan.

### **Early Reaction to the *Deere* Decision**

Shortly after the decision was issued, a number of ERISA practitioners discussed the ruling with BNA and offered their own opinions on what the decision could mean for plan fees cases in particular and fiduciary breach claims in general (42 PBD, 3/6/09; 36 BPR 589, 3/10/09).

Some in the plaintiffs' bar were particularly concerned with the Seventh Circuit's decision to uphold the lower court's dismissal of the case with prejudice. Among other things, there was concern at the time that the *Deere* decision would shift the burden of determining the appropriateness of plan investments and the reasonableness of the fees squarely on the plaintiffs' shoulders.

Still others in the plaintiffs' bar were concerned that the Seventh Circuit never mentioned the “process” by which *Deere* selected its plan investments and instead focused only on the fact that the *Deere* plan offered a large number of investment options.

On the other side of the aisle, a number of attorneys from the defendants' bar said they were pleased with the outcome of the case. Some pointed out that the Seventh Circuit's decision recognized that there is no “one-size-fits-all” approach to prudence when it comes to the selection of plan investments.

But others in the defendants' bar voiced concerns over the steps the Seventh Circuit used to reach its decision. Some were concerned at the time that the Seventh Circuit was endorsing a view that plan fiduciaries could be insulated from liability simply by offering a large number of investment options in a plan without actually considering whether the investments were proper.

### **Seventh Circuit Refuses to Rehear Case**

Within weeks of the Seventh Circuit's decision, a motion for a panel rehearing was filed by the plaintiff plan participants. The plaintiffs' motion for a rehearing was soon followed by similar requests from the Secretary of Labor, AARP, the National Senior Citizens Law Center, the Pension Rights Center, Fund Democracy Inc., the Consumer Federation of America, and five law school professors (72 PBD, 4/17/09; 36 BPR 967, 4/21/09)

Four months after the Seventh Circuit issued the *Deere* decision, the court announced that it would not take a second look at the case. But rather than simply issuing an order denying a rehearing of the case, the Seventh Circuit took steps to address several points of criticism that were raised after it issued its decision in February (121 PBD, 6/26/09; 36 BPR 1567, 6/30/09).

One point of criticism addressed in the Seventh Circuit's order was the Secretary of Labor's contention that the *Deere* panel erred by failing to give appropriate deference to her interpretation of the regulation implementing ERISA Section 404(c). The Seventh Circuit in its order said that the three-judge panel did not simply ignore language in the regulation. In fact, the Seventh Circuit said the three-judge panel had deferred to the secretary's concerns about Section 404(c) to the extent that the panel refrained from making any definitive pronouncement on whether the Section 404(c) safe harbor applies to the selection of investment options for a plan.

In addition, the Seventh Circuit disposed of the secretary's perceived “fear” that the three-judge panel's decision in *Deere* could be read as a sweeping statement that any plan fiduciary could insulate itself from liability by simply including a large number of investment options in the plan.

In October, the plaintiffs in the *Deere* case filed a petition asking the U.S. Supreme Court to review the Seventh Circuit's decision. The Supreme Court has not yet acted on the petition.

### **The Eighth Circuit's Turn in *Wal-Mart***

In the aftermath of the *Deere* decision, there was some concern as to whether other federal courts would follow the same path and dismiss similar plan fees cases. That concern was recently put to rest when the U.S. Court of Appeals for the Eighth Circuit took a different approach to a similar plan fees case.

*Braden v. Wal-Mart Stores Inc.*, 48 EBC 1097 (8th Cir. 2009), presented the Eighth Circuit with some of the same issues that were raised in the *Deere* case (226 PBD, 11/30/09; 36 BPR 2743, 12/1/09). And like the *Deere* case, the *Wal-Mart* lawsuit took the fast track and was dismissed by a federal court just months after the lawsuit was filed and

before discovery could take place (225 PBD, 11/21/08; 35 BPR 2666, 11/25/08; 45 EBC 1597).

Wal-Mart employee Jeremy Braden alleged in his lawsuit that Wal-Mart's Section 401(k) plan, which is one of the largest Section 401(k) plans in the country, paid somewhere between \$62 million and \$92 million in fees to the plan's service providers between January 2002 and early 2008. Wal-Mart's plan offers participants 10 mutual funds that were retail class shares, which generally are more expensive than institutional class shares available to large retirement plans.

Braden alleged that the plan's fiduciaries failed to prudently and loyally evaluate the investment options for the participants and that they instead selected unreasonably expensive mutual funds that substantially diminished the retirement savings of plan participants.

He further alleged that the fiduciaries engaged in prohibited transactions under ERISA by allowing plan assets to be paid to the plan's trustee, Merrill Lynch & Co., in the form of revenue-sharing payments. In addition, Braden claimed that the fiduciaries breached their duties by failing to completely and accurately inform the plan's participants about the impact the mutual funds' excessive fees had on their retirement savings.

In dismissing Braden's complaint, the district court said Braden's complaint did not allege that Wal-Mart and the plan fiduciaries failed to use a prudent process in selecting the plan's investment options. The district court added that Braden had made conclusory allegations, without any factual support, that the fiduciaries did not analyze options or use a proper process to investigate the merits and structure of the plan's investment choices.

In addition, the district court dismissed Braden's claim that Wal-Mart and the fiduciaries breached their duties by failing to tell plan participants about revenue-sharing payments being made to the plan's trustee, Merrill Lynch. The court also nixed Braden's claim that Wal-Mart engaged in prohibited transactions by making revenue-sharing payments to Merrill Lynch.

### **Lawsuit Against Wal-Mart Reinstated**

On Nov. 25, the Eighth Circuit vacated the district court's dismissal of Braden's lawsuit and sent the case back to the district court for trial.

The Eighth Circuit ruled that:

- The district court erred when it found that Braden lacked standing to maintain claims for the period before he began participating in Wal-Mart's plan. The Eighth Circuit said Braden had satisfied the requirements for standing under ERISA and Article III of the U.S. Constitution.
- The district court's dismissal of Braden's lawsuit was based on a flawed interpretation of the pleading requirements of Rule 8 of the Federal Rules of Civil Procedure. According to the appeals court, the district court ignored reasonable inferences supported by the facts alleged in Braden's complaint and instead drew inferences in favor of Wal-Mart, faulting Braden for failing to plead facts tending to contradict those inferences.
- The lower court erroneously dismissed Braden's claim that the plan fiduciaries breached their duties by not disclosing the plan fees and revenue-sharing payments. The Eighth Circuit said that while there is no per se duty to disclose revenue-sharing payments, Braden had alleged sufficient facts to support an inference that nondisclosure of the fees and revenue-sharing payments would preclude participants from making adequately informed investment decisions.
- The district court incorrectly dismissed Braden's prohibited transaction claim by finding that he had failed to plead facts raising a plausible inference that the payments Wal-Mart made to Merrill Lynch were unreasonable in relation to the services provided by Merrill Lynch. The Eighth Circuit said Braden did not have the burden of pleading facts that would show that the revenue-sharing payments were unreasonable in proportion to the services rendered by Merrill Lynch. The court pointed out that it would have been impossible for Braden to show without discovery that the revenue-sharing payments were unreasonable because the trust agreement between Wal-Mart and Merrill Lynch required that the revenue-sharing amounts be kept secret.

### **Deere Mentioned in Two Footnotes**

The Eighth Circuit took steps to recognize the Seventh Circuit's decision in *Deere*, but limited its discussion of *Deere* to two footnotes.

In one footnote, the Eighth Circuit compared the *Deere* decision by pointing out that in that case, Deere had offered its participants over 2,500 mutual funds that had a variety of expense ratios. The Eighth Circuit said the case against Wal-Mart differed from *Deere* because Wal-Mart's plan offered a far narrower range of investment options, which made it "more plausible" that the plan was imprudently managed by Wal-Mart.

In a second footnote, the Eighth Circuit echoed the Seventh Circuit by saying that it was not suggesting that a fiduciary breach exists when there is a bare allegation that a cheaper alternative investment exists in the marketplace. Citing *Deere*, the Eighth Circuit said it was "clear" that "nothing in ERISA requires every fiduciary to

scour the market to find and offer the cheapest possible fund.' "

### Early Reaction to *Wal-Mart*

The day the *Wal-Mart* decision was released, Braden's attorney—Derek Loeser of Keller Rohrback, Seattle—issued a press release saying the Eighth Circuit's decision was an "important step" in Braden's effort to pursue ERISA claims on behalf of *Wal-Mart* employees whose retirement benefits are at risk due to *Wal-Mart*'s failure to act in the best interests of its employees.

"We look forward to the opportunity to make our case that *Wal-Mart* should have used its massive bargaining power for the benefit of its employees through the selection of reasonably priced funds, rather than retail off-the-shelf funds that are chosen because of financial incentives that benefit the Plan Trustee Merrill Lynch. The 401(k) plan has become the primary retirement vehicle for Americans and it is incumbent upon plan fiduciaries to think in terms of what is best for plan participants not what is best for financial institutions that profit from the plans," Loeser said.

Shortly after the Eighth Circuit released the *Wal-Mart* decision, the Minneapolis law firm Dorsey & Whitney, which represents employers and management in ERISA litigation, posted to its website an article that examined what the decision would mean for employers.

The article, written by attorneys Stephen P. Lucke and Andrew Holly, said that the *Wal-Mart* decision "lowers the bar for class action attorneys to bring claims alleging that 401(k) plans charge and improperly disclose excessive fees."

The two attorneys said the case "should prompt employers to review how they administer their 401(k) plans." According to the article, the decision is a "flashing yellow light" cautioning employers that:

- It is now easier for plaintiffs to proceed to discovery based on allegations that Section 401(k) fiduciaries should have offered investment options with lower fees, particularly for large plans that allegedly failed to take full advantage of their market power.
- Notwithstanding recent court rulings holding that ERISA imposes no affirmative duty to disclose to participants the plan's revenue-sharing arrangements, employers and fiduciaries are now more vulnerable to such claims and should review what their plan communications say about fees.
- Even if revenue-sharing amounts are reasonable and used to defray recordkeeping expenses, the increased possibility that they can form the basis for a prohibited transaction claim that proceeds to discovery may cause plans to reconsider how they use and disclose revenue sharing.

### Comparing and Contrasting

#### *Deere* and *Wal-Mart*

When asked by BNA whether the number of investment options offered under the *Deere* and *Wal-Mart* plans had an impact on the appeals courts' decisions, attorney Gary Tell of O'Melveny & Myers, Washington, D.C., told BNA Dec. 2 that the cases should not be distinguished by the number of investments offered under the plans.

Tell, who represents employers and management in ERISA litigation, said that in *Deere* the sheer number of funds offered by the *Deere* plan with its BrokerageLink option "seemed to have given the Seventh Circuit some comfort," but that does not mean that numbers alone matter in these cases.

"What really matters in these cases is whether participants have the ability to choose funds with a range of expense ratios that are set in a competitive market environment," Tell said.

Tell also pointed out that both the Seventh and Eighth Circuits cited to the U.S. Supreme Court's decision in *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007), dealing with the plausibility standard that applies in order for complaints to survive a motion to dismiss. He said that while both courts cited to *Twombly*'s plausibility standard, the court in *Deere* relied more heavily on materials outside of the four corners of the complaint, like plan documents, trust agreements, and fund prospectuses.

"The Seventh Circuit spilled considerable ink concluding that the district court's use of those documents was proper. The Eighth Circuit focused more heavily on the complaint's allegations and was willing to draw plaintiff-friendly inferences from them," Tell said.

In his observations about the *Wal-Mart* decision, attorney Andrew Oringer of Ropes & Gray, New York, told BNA Dec. 2 that the Eighth Circuit paid "specific lip service" to the notion that selecting investments for a Section 401(k) plan is paramount. "But then, the court seems to view facts that it intuitively regards as disturbing as giving rise to a reasonable inference that the process was flawed," Oringer said.

The Eighth Circuit worried that *Wal-Mart*'s selection process may have been tainted by a "failure of effort, competence, or loyalty," but the allegations of any lack of effort were unclear, Oringer said. Oringer is a partner with Ropes & Gray and advises employers on employee benefit, tax, and executive compensation issues. He is also an adjunct professor at Hofstra University School of Law.

Plaintiffs' attorney Ellen Doyle of Stember Feinstein Doyle & Payne, Pittsburgh, told BNA Dec. 3 that the number of investment options offered under a Section 401(k) plan should not be the determinative factor on a motion to dismiss.

"Participants believe that ERISA sets a prudent man standard of care for the selection of plan investments offered for employees' contributions. Whether there are 13 investment options provided as in the *Wal-Mart* case or 2,500 as there were in the *Deere* case should not be dispositive on a motion to dismiss. Yet the *Deere* case placed a great deal of emphasis on the fact that there were so many investment options available through a brokerage window offered by the *Deere* plan," Doyle said.

She added that the Seventh Circuit considered the number of funds offered to be significant. "Participant representatives were concerned that courts not dilute the standard of care in the selection of investment options by allowing fiduciaries to simply offer a lot of funds without fiduciary consideration. That concern was expressly addressed by the Seventh Circuit in its reconsideration opinion where it stated that its opinion was not such a sweeping assertion and that the plaintiffs in the case had not argued that any of the 26 funds offered directly were unsound or reckless," Doyle said.

### **The Section 404(c) Distinction**

Plaintiffs' attorney Gregory Y. Porter of Bailey & Glasser, Washington, D.C., told BNA Dec. 3 that the major distinction between the *Wal-Mart* and *Deere* cases was that ERISA Section 404(c) was addressed in *Deere* while it was not at issue in *Wal-Mart*.

Porter said that while the Seventh Circuit discussed at length the number of investment options offered under *Deere's* plan, the court did so in the context of its discussion of the ERISA Section 404(c) defense. While the Eighth Circuit addressed *Deere* in a footnote, ERISA plans in the Eighth Circuit "can't take too much comfort" with the Eighth Circuit's decision since the *Wal-Mart* case did not deal with Section 404(c), Porter said.

Porter added that the *Wal-Mart* case focused more on whether the plan fiduciaries used due diligence in the investment selection process. At the end of the day, the question is not about the number of funds offered by Section 401(k) plans, but rather whether the plan fiduciaries "did their job up front" by prudently selecting investments for the plan, Porter said.

He added that in *Deere*, the Seventh Circuit did not focus on the investment selection process because the court did not buy the notion that the fiduciaries had a threshold duty to ensure that the fund line-up was prudent. Porter said the Seventh Circuit ignored the fact that when a fiduciary offers a line-up of funds, the selection is viewed as an implicit endorsement of those funds by the plan fiduciaries.

### **Circuit Split on Revenue Sharing?**

The Seventh and Eighth Circuits also reached different conclusions on whether revenue sharing must be disclosed under ERISA. The Seventh Circuit said that there is never a duty to disclose revenue sharing, but the Eighth Circuit said disclosure might be required if information about revenue sharing would assist plan participants in making their investment choices.

Attorney Tell said that while the two courts looked to the revenue-sharing disclosure issues quite differently, the opposing views by the courts does not necessarily mean there is a circuit split as an analytical matter. "The Eighth Circuit was willing to draw inferences from the allegations in the complaint and kick the can down the road. Of course, the plaintiffs will still have to prove their case. And it's not clear what relief is available for a disclosure claim like this," Tell said.

Attorney Lucke likewise said that it is not entirely clear whether the Eighth Circuit's discussion of revenue sharing would qualify as a circuit split.

"*Wal-Mart* was not entirely clear about when circumstances would arise that would trigger a duty to disclose more information about fees or revenue sharing, so this will likely be an issue for future litigation. Whether *Wal-Mart* has resulted in a circuit split or just reflects tension between the two circuits is something litigants will argue about," Lucke told BNA Dec. 2.

Oringer said he thought the discussion in the *Wal-Mart* case was "unfortunate" and missed the distinction between information that is of value to a fiduciary and information that may be of value to a participant. "I think *Deere* got this one right," Oringer said.

Plaintiffs' attorney Porter agreed that the revenue-sharing issue separated the two decisions and said that the Eighth Circuit's ruling recognized that a fiduciary breach claim could exist if there are sufficient allegations that compensation paid in revenue sharing was really nothing other than "pay-to-play" instead of for actual services rendered by the plan service providers.

### **Pleading Standards**

As an attorney who often represents plaintiffs in ERISA cases, attorney Porter told BNA that aside from the plan fees issues, the Eighth Circuit's ruling in *Wal-Mart* could bring a sea change for ERISA pleadings in general.

Porter said that the Eighth Circuit's decision makes it clear that an ERISA plaintiff does not have to rebut every plausible defense theory in order to state an ERISA fiduciary breach claim. "This applies to plaintiffs' cases across the board, not just ERISA or plan fees cases," Porter said.

In addition, Porter said the Eighth Circuit's decision opened the door for the use of circumstantial evidence in ERISA pleadings. The Eighth Circuit recognized that ERISA plaintiffs should be able to use circumstantial evidence and this recognition brings implications for all fiduciary breach cases in the Eighth Circuit because circumstantial evidence is enough now to allege a breach, Porter said.

### Two Decisions From the Second Circuit

The Seventh and Eighth Circuits were not alone in 2009 in dealing with the plan fees cases. On two occasions, the Second Circuit took on plan fees cases and in both situations the court in nonprecedential, summary orders upheld the dismissal of the cases. Because of the nonprecedential and summary nature of the two cases, it is unclear whether the Second Circuit has taken a firm position in the cases.

The cases, which both went in favor of the defendants, have drawn considerably less attention than the *Deere* and *Wal-Mart* cases.

The first case by the Second Circuit was *Young v. General Motors Investment Management Corp.*, 46 EBC 2278 (2d Cir. 2009)(86 PBD, 5/7/09; 36 BPR 1150, 5/12/09).

The case came up to the Second Circuit after the U.S. District Court for the Southern District of New York ruled in March 2008 that the plan participants were time-barred from pursuing their claim that General Motors Investment Management Corp. (GMIMC) breached its fiduciary duties by investing in mutual funds that carried fees in excess of similar investments (61 PBD, 3/31/08; 35 BPR 732, 4/1/08; 43 EBC 3000).

In affirming the lower court's dismissal of the lawsuit, the Second Circuit shifted focus from the statute of limitations issue and instead looked to whether the case should have been dismissed for failure to state a claim on which relief could be granted.

In its decision, the appeals court said the participants' excessive fees claim would not have survived GMIMCO's motion to dismiss, even if the claim had been timely. The Second Circuit applied the standard for excessive fees articulated in the context of the Investment Company Act, which requires an allegation that an adviser-manager charged a fee that was so disproportionately large that it bore no reasonable relationship to the services rendered and could not have been the product of arm's-length bargaining.

According to the Second Circuit, the participants failed to allege that the fees were excessive relative to the services rendered and they also did not allege any other factors relevant to determining if the fees were excessive under the circumstances.

### No Rationale for Decision

Later in 2009, the Second Circuit was again confronted with a Section 401(k) plan fees case in *Taylor v. United Technologies Corp.*, (2d Cir. 2009)(228 PBD, 12/2/09). The Second Circuit took the same approach it had taken in the *General Motors Investment Management* case by issuing an unpublished decision. But unlike the *General Motors Investment Management* case where the Second Circuit gave some rationale for its decision, in *United Technologies* the Second Circuit merely said it agreed with the lower court's "thorough and well-reasoned" decision.

In their lawsuit, three participants in the United Technologies Corp.'s Section 401(k) plan claimed that UTC and the plan's fiduciaries breached their duties by: (1) holding too much cash in the UTC stock fund instead of investing the money in UTC stock, (2) paying excessive recordkeeping and administrative fees to the plan's recordkeeper, and (3) making misrepresentations about the fees and expenses charged by Fidelity.

In March 2009, the U.S. District Court for the District of Connecticut granted summary judgment in favor of UTC on all claims (41 PBD, 3/5/09; 36 BPR 565, 3/10/09; 46 EBC 1935).

First, the district court said UTC did not breach its fiduciary duties by having its UTC Stock Fund hold a substantial amount of cash rather than stock. According to the court, UTC retained a sufficient amount of cash in the stock fund to provide transactional liquidity as participants sold their UTC stock.

Next, the district court rejected the participants' contention that UTC's selection of investments was imprudent because it should have engaged in extensive investigation prior to selecting actively managed mutual fund given the "near certainty" that an actively managed mutual fund would not outperform lower-fee index funds.

The court said that in selecting the actively managed mutual funds, UTC underwent a detailed evaluation and analytical process to determine whether to include such funds in the plan.

Likewise, the district court said that even if the participants put forth evidence that UTC could have selected a less-costly option, the evidence demonstrated that UTC's investment selection process "included consideration of the fees charged on the mutual fund options, and of the returns of each mutual fund net of its management expenses."

The district court also was unpersuaded by the participants' argument that UTC breached its fiduciary duties by allowing the plan to pay unreasonably high compensation to Fidelity. The court found, among other things, that there was no evidence that Fidelity's receipt of the negotiated base fee and sub-transfer agent fees was "materially unreasonable and beyond the market rate." Instead, the court said there was evidence that other service providers would have charged comparable sub-transfer fees.

In addition, the court rejected the participants' assertion that UTC breached its fiduciary duties by failing to disclose that the participants, rather than UTC, paid fees to Fidelity.

In their appeal, the participants argued that the district court erred in granting summary judgment in favor of UTC. The participants maintained that their evidence showed that: (1) UTC chose retail mutual funds as investment options for employees without considering the deficiencies of mutual funds for large retirement plans, as compared to alternatives more suited to large retirement plans; (2) UTC's mutual funds deducted from participant investments unreasonably high sub-transfer fees; (3) UTC did not disclose full information about the sub-transfer fees and failed to investigate or otherwise account for the allegedly excessive amount being paid; and (4) UTC operated the employee stock fund imprudently, causing significant underperformance.

In its summary order, the Second Circuit said it found the participants' arguments to be without merit.

### Sampling of Pro-Plaintiff Decisions

While there was a significant amount of attention paid to the appellate-level plan fees cases in 2009, a number of federal district courts were also at work dealing with the cases. The following cases were decided in favor of plaintiffs:

- A federal court in Minnesota in March denied Wells Fargo & Co.'s motion to dismiss a lawsuit by employees who claimed that the company breached its fiduciary duties and engaged in prohibited transactions by investing the company's Section 401(k) plan in mutual funds managed by a Wells Fargo affiliate. The court said it was too early in the litigation to dismiss the employees' lawsuit because they had set forth sufficient allegations that Wells Fargo breached its fiduciary duties (*Gipson v. Wells Fargo & Co.*, 46 EBC 1391 (D. Minn. 2009)(48 PBD, 3/16/09; 36 BPR 639, 3/17/09)).
- The trustees of as many as 24,000 pension plans that invested in variable annuity contracts issued by Nationwide Financial Services Inc. and Nationwide Life Insurance Co. were certified as a class by the U.S. District Court for the District of Connecticut in a long-running case that challenges the Nationwide companies' collection of revenue-sharing payments (*Haddock v. Nationwide Financial Services Inc.* (D. Conn. 2009)(215 PBD, 11/10/09; 36 BPR 2590, 11/17/09)).
- Caterpillar Inc. agreed in November to pay \$16.5 million as part of a settlement resolving claims that it breached its fiduciary duties by including retail mutual funds in its Section 401(k) plan even though the plan was allegedly large enough to demand investment management through low-cost institutional structures. The lawsuit had also alleged that Caterpillar's plans paid excessive fees to a caterpillar subsidiary known as Caterpillar Investment Management Ltd. (*Martin v. Caterpillar Inc.* (C.D. Ill. 2009) (214 PBD, 11/9/09; 36 BPR 2595, 11/17/09)).

### Sampling of Pro-Defendant Decisions

There were at least three significant pro-defendant decisions by the federal district courts in 2009. The decisions include:

- A federal court in California ruled that Southern California Edison and its parent company, Edison International, did not violate ERISA's prohibited transaction rules by entering an agreement with Hewitt Associates LLC that allowed for Hewitt's recordkeeping costs to be paid in part by revenue-sharing payments Hewitt received from mutual funds offered under the companies' Section 401(k) plan. However, the district court refused to rule on whether the plan's fiduciaries breached their ERISA duties by selecting retail mutual funds in order to maximize the amount of revenue-sharing payments that would be received by Hewitt, which would in turn reduce the recordkeeping fees the companies would owe to Hewitt (*Tibble v. Edison Int'l*, 47 EBC 2363 (C.D. Cal. 2009)(145 PBD, 7/31/09; 36 BPR 1824, 8/4/09)).
- The U.S. District Court for the Southern District of Ohio dismissed as time-barred a lawsuit by Fifth Third Bancorp employees who claimed that the company and its top officials breached their fiduciary duties by "loading" the company's Section 401(k) plan with several Fifth Third mutual funds that charged excessive and unreasonable fees. The court found that the employees had filed their excessive fees-related claim just two weeks after the three-year statute of limitations had expired (*Shirk v. Fifth Third Bancorp*, 47 EBC 2523 (S.D. Ohio 2009)(191 PBD, 10/6/09; 36 BPR 2351, 10/13/09)).
- Honda of America Manufacturing Inc. convinced a federal court in Ohio to dismiss a lawsuit by Honda employees who claimed the automaker breached its ERISA fiduciary duties by loading its Section 401(k) plan with investment funds that charged excessive fees. The court, relying heavily on the Seventh Circuit's *Deere* decision, said the employees had failed to state a claim upon which relief could be granted. Four days later, the district court dismissed similar excessive fees claims the Honda employees lodged against the plan's trustee, Merrill Lynch Bank & Trust Co. (*In re Honda of America Mfg. Inc. ERISA Fees Litigation*, 47 EBC 2610 (S.D. Ohio 2009)(197 PBD, 10/15/09; 36 BPR 2397, 10/20/09)).

### Mixed Ruling in *Lockheed* and the Future of Class Actions

At least one plan fees case from 2009 ended with a mixed ruling. In March, the U.S. District Court for the Southern District of Illinois ruled that employees of Lockheed Martin Corp. could go forward, in part, with their claims that Lockheed breached its fiduciary duties by selecting retirement plan investment options that allegedly charged unreasonably high fees (*Abbott v. Lockheed Martin Corp.*, 46 EBC 1914 (S.D. Ill. 2009)(61 PBD, 4/2/09; 36 BPR 850, 4/7/09).

In that case, the district court denied Lockheed's motion for summary judgment on three claims. Those claims include allegations that Lockheed breached its fiduciary duties by: (1) failing to ensure that plan participants were not harmed by excessive overall fees, (2) failing to administer the Stable Value Fund to ensure that it was a prudent investment option, and (3) imprudently diluting returns in the company stock funds by unnecessarily holding cash or holding excessive amounts of cash in the funds.

However, the district court granted summary judgment in favor of Lockheed on claims that it breached its duties by: (1) failing to monitor revenue-sharing payments made between the company's pension plans and the plans' service providers, and (2) offering a high-cost retail mutual fund in the plan which allegedly could have saved the plan as much as \$41.25 million in fees if it had not been offered under the plan.

### Testing Class Certification Post-*LaRue*

Another important development in 2009 arose in the Seventh Circuit when the appeals court in July decided to consolidate for appeal four ERISA lawsuits, two of which involve excessive fees claims (158 PBD, 8/19/09; 36 BPR 1962, 8/25/09). The two excessive fees cases involved in the consolidated appeal are *Spano v. Boeing Co.* (7th Cir., No. 09-3001) and *Beesley v. International Paper Co.* (7th Cir., No. 09-3018).

Each of the appeals asked the Seventh Circuit to determine what effect, if any, the U.S. Supreme Court's decision in *LaRue v. DeWolff, Boberg & Associates*, 128 S. Ct. 1020, 42 EBC 2857 (2008)(34 PBD, 2/21/08; 35 BPR 467, 2/26/08), had on the lower courts' grant of class action status.

In general, the appeals all raise the issue of whether class certification is appropriate in situations where fiduciary breaches allegedly cause losses to the individual accounts of Section 401(k) participants, as opposed to situations where systemic breaches cause losses to the entire plan rather than individual accounts.

The *Boeing* and *International Paper* plan fees cases were certified as class actions by the U.S. District Court for the Southern District of Illinois in late-2008 (190 PBD, 10/1/08; 35 BPR 2295, 10/7/08; 191 PBD, 10/2/08; 35 BPR 2295, 10/7/08). After the court certified the cases as class actions, Boeing and International Paper filed appeals to the Seventh Circuit arguing that *LaRue* foreclosed on any right the participants had to seek class certification of their ERISA breach claims.

The same day the Seventh Circuit announced that it would consolidate the appeals, the Southern District of Illinois issued orders staying the *Boeing* and *International Paper* cases pending the appeal. Recently, however, the district court lifted the stay in the *International Paper* case and said it could proceed to trial even though the Seventh Circuit has not yet decided whether the case should have been certified as a class action (229 PBD, 12/3/09).

### What's Next?

The plan fees decisions from 2009 have left many guessing what the future holds for these cases.

Attorney Tell, in making a general observation about all of the Section 401(k) plan fees cases, told BNA that the courts have not welcomed the plaintiffs' "generic attacks" on Section 401(k) plan administration. "These would include allegations that plan fiduciaries must avoid retail mutual funds, sector funds, unitized stock funds, and other common features that the plaintiffs suggested were walking violations of the law," Tell said.

"Courts recognize that there isn't a legally mandated, off-the-rack investment structure. Fiduciaries require maneuvering room to satisfy the needs of their plan's participants," Tell added.

Attorney Oringer told BNA that the outcome in some of the cases is leading to a "troubling trend" of courts increasing a fiduciary's level of insulation from liability if the fiduciary provides for a wide-open menu of investments.

"There's nothing necessarily wrong with a fiduciary wanting to open up the menu, but it would be awful if ERISA eventually came to be read to be an encouragement to abrogating fiduciary duties in favor of a do-whatever-you-want approach. Indeed, *Wal-Mart* says point blank that a relatively narrow range of investment options makes a claim of imprudence more plausible," Oringer said.

Oringer added that a plan fiduciary should be free, "and maybe encouraged," to provide a pared down set of investment alternatives so as to try to mitigate the confusion of a virtually infinite number of choices.

"Sometimes you want the neverending menu at Friday's or The Cheesecake Factory, and sometimes you don't. Sometimes, less is more. Unfortunately, after *Wal-Mart*, employers may feel less comfortable with that approach. The point is, a company should be able to go in either direction—a tailored menu or an open-ended approach—depending on what it thinks is best for its workforce," Oringer said.

By Jo-el J. Meyer

### What Are Plan Fees Cases?

The "plan fees" cases, as they are often referred to by ERISA practitioners, take aim at the fees and costs that Section 401(k) plan participants pay for investments offered under their plans. The claims often allege that the fees were unreasonable or excessive in light of the investment services received. Often there will also be claims that the service providers engaged in the practice of revenue sharing. In addition, the lawsuits will often allege that the plans' sponsors should have bargained for a better deal on the plan fees in light of the plans' large size.

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