EBEC EXPO2024

Proskauer's Perspective on Employee Benefits, Executive Compensation and ERISA Litigation

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Current Developments in ERISA Litigation

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Meet Your Presenters

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Agenda

- Actively Litigated Claims
  - 401(k) & 403(b) plans: Excessive recordkeeping fees, excessive investment fees, and investment underperformance
  - Defined benefit plans: Use of outdated actuarial assumptions to calculate QJSAs
- Claims to Watch
  - Health plans: Claims by plans and participants
  - Defined benefit plans: Pension risk transfers

Actively Litigated Claims

401(k) Plan Fees and Performance: Common Claims

- Recordkeeping Fees
  - Fees exceed fees paid by other plans
- Investment Claims
  - Excessive investment management fees
    - Active/passive investment strategies
    - Mutual funds vs. collective investment trusts vs. separate accounts
    - Exceeds median fees reported by the Investment Company Institute
    - Share class selection
    - Cheaper, similar options available
  - Untested or underperforming funds

401(k) Plan Fees and Performance: Key Statistics

	2023	2022
New Complaints	48	82
Motion to Dismiss Decisions	76 [31 granted, 22 denied, 23 granted in part]	60 [23 granted, 20 denied, 17 granted in part]
Class Certification	17 [6 stipulated classes]	16 [10 stipulated classes]
Motion for Summary Judgment Decisions	12 [3 granted, 6 denied, 3 granted in part]	5 [2 granted, 2 denied, 1 granted in part]
Appellate Decisions	7	9
Trials	4 [first jury trial]	0
Settlements	$261,000,000	$151,220,000

401(k) Plan Fees and Performance: *Hughes v. Northwestern Univ.*

- 401(k) plan participants claimed that the plan fiduciaries allegedly agreed to excessive recordkeeping fees, offered mutual funds with excessive management fees, and offered too many investment options.
- The Supreme Court held that the availability of many unchallenged investments does not absolve plan fiduciaries of the duty to remove imprudent investment options within a reasonable time.
- While most viewed *Hughes* as a non-event, there were some positive statements for plan fiduciaries:
    - Because the content of the duty of prudence turns on the circumstances prevailing at the time the fiduciary acts, “the appropriate inquiry will necessarily be context specific.”
    - “At times, the circumstances facing an ERISA fiduciary will implicate difficult tradeoffs and courts must give due regard to the range of reasonable judgments a fiduciary may make based on her experience and expertise.”

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401(k) Plan Fees and Performance: Post-*Hughes* Developments

- In evaluating motions to dismiss, most courts look at whether plan participants have pled the existence of meaningful benchmarks.
- For claims alleging excessive recordkeeping fees:
  - Are the plans receiving the same range of services?
- For claims alleging excessive investment fees or underperformance:
  - Do the investments have similar strategies, styles, objectives, risk profiles, and potential rewards?
- The circuit court's context-specific evaluation of plaintiffs' allegations of meaningful benchmarks has resulted in some cases being dismissed while others have proceeded into discovery. The reasons for the different outcomes are not easy to discern.

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401(k) Plan Fees and Performance: Post-*Hughes* Developments *cont'd*

- Several circuit courts have dismissed claims for failing to plead specific facts that support the validity of plaintiffs' comparisons.
  - *Forman v. TriHealth*, 40 F.4th 443 (6th Cir. 2022)
    - Plaintiffs alleged that the recordkeeping fees were 2x greater than their comparator plans, but the Sixth Circuit determined that they failed to allege that the fees were high in relation to the services offered.
    - Plaintiffs alleged that the comparator investments were in the same investment style as challenged funds, but the Sixth Circuit determined that they never alleged that the fees associated with actively managed funds (as opposed to passively managed funds) could not be justified by the plan's strategic goals.
  - *Albert v. Oshkosh*, 47 F.4th 570 (7th Cir. 2022)
    - While plaintiffs alleged that the recordkeeping fees for the target plan were approximately 2x greater than their similarly-sized comparator plans, the Seventh Circuit determined that they failed to plead details regarding the kinds of services the plans received.
    - The Seventh Circuit also dismissed plaintiffs' allegations that defendants failed to consider materially similar, less expensive investment options because, standing alone, there was no meaningful comparison between the actively-managed and passively-managed investment options.

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401(k) Plan Fees and Performance: Post-*Hughes* Developments

- *Matousek v. MidAmerican*, 51 F.4th 274 (8th Cir. 2022)
  - While plaintiffs alleged that the recordkeeping fees for the target plan were approximately 4x greater than their similarly-sized comparator plans, the target plan's expenses included a broad suite of services while the comparator plans only received a basic suite of services.
  - Plaintiffs failed to support their allegations of excessive investment fees and underperformance with information about their comparators, *e.g.*, whether they held similar securities, had similar investment strategies, and reflected a similar risk profile, or in some cases pointed to alleged benchmarks with different strategies.
- *Matney v. Barrick Gold*, 80 F.4th 1136 (10th Cir. 2023)
  - The Tenth Circuit ruled that merely alleging that CITs are less expensive—without any information about their aims, risks, and potential rewards—was conclusory and not sufficient to establish a meaningful comparison.
  - The Tenth Circuit also ruled that plaintiff failed to offer factual allegations about the recordkeeping services provided to the plan relative to his comparator plans or industry averages.

401(k) Plan Fees and Performance: Post-*Hughes* Developments *cont'd*

- Other circuit courts have determined that, in their view, plaintiffs' allegations of excessive fee and investment underperformance were plausible based on valid comparisons.
  - *Perkins v. United Surgical*, 2024 WL 1574342 (5th Cir. 2024)
    - The Fifth Circuit ruled that plaintiffs' allegations of excessive recordkeeping fees were supported with meaningful benchmarks
      - Plaintiffs alleged that the plan's costs were more than 2.5x the costs for similar-sized plans; and
      - There were sufficient details about the services offered by the target plan and how they were similar to those offered by plaintiffs' comparator plans.
  - *Sweda v. University of Pennsylvania*, 923 F.3d 320 (3d Cir. 2019)
    - The Third Circuit determined that plaintiff plausibly alleged a claim based on including and retaining high-cost investment options with historically poor performance compared to other options, in part, because plaintiff alleged that 60% of plan options underperformed "appropriate benchmarks."

401(k) Plan Fees and Performance: Post-*Hughes* Developments *cont'd*

- And at least one circuit court has green-lighted plaintiffs' claims to proceed by declining to require factual support that comparisons are meaningful.
  - *Davis v. Salesforce.com*, 2022 WL 1055557 (9th Cir. 2022)
    - Plaintiffs did not need to allege facts supporting the comparability of mutual funds and CITs because that is a factual issue not to be resolved on a motion to dismiss.
    - It was sufficient that plaintiffs alleged that the CITs had the same underlying investments and asset allocations as their mutual fund counterparts but had better annual returns and a lower net expense ratio.

401(k) Plan Fees and Performance: share class claims

- Plaintiffs have withstood motions to dismiss claims that defendants imprudently offered the retail share class of a mutual fund with higher fees when they could have offered the institutional share class of the same mutual fund with lower fees.
- This "claim is special in that the comparator action that a prudent fiduciary should have taken—replacing retail shares with institutional shares—is baked into the claim." *Hughes v. Nw. Univ.*, 63 F.4th 615 (7th Cir. 2023); *see*
  - *Perkins v. United Surgical*, 2024 WL 1574342 (5th Cir. 2024);
  - *Forman v. TriHealth, Inc.*, 40 F.4th 443 (6th Cir. 2022);
  - *Kong v. Trader Joe's Co.*, 2022 WL 1125667 (9th Cir. 2022);
  - *Davis v. Salesforce.com*, 2022 WL 1055557 (9th Cir. 2022);
  - *Sacerdote v. N.Y. Univ.*, 9 F.4th 95 (2d Cir. 2021);
  - *Davis v. Wash. Univ. in St. Louis*, 960 F.3d 478 (8th Cir. 2020);
  - *Sweda v. Univ. of Pa.*, 923 F.3d 320 (3d Cir. 2019).

401(k) Plan Fees and Performance: Prohibited Transaction Claims

- ERISA section 406(a)(1)(C) provides that a plan fiduciary shall not cause the plan to engage in a transaction, if the plan fiduciary knows or should know that such transaction constitutes a direct or indirect furnishing of goods or services between the plan and a party in interest.
- ERISA section 408(b)(2) states that the prohibitions provided in section 406 do not apply to reasonable arrangements with a party in interest for services necessary to the establishment or operation of the plan if no more than reasonable compensation is paid therefor.
- Circuit courts are split on the pleading requirement for prohibited transaction claims.

401(k) Plan Fees and Performance: Prohibited Transaction Claims

- Two circuit courts have permitted ERISA section 406(a)(1)(C) claims to proceed without allegations as to the reasonableness of fees:
  - Eighth Circuit: Plaintiffs alleged that the plan sponsor caused the plan to enter into an agreement with a party in interest in which it received undisclosed amounts of revenue sharing payments in exchange for services rendered. Plaintiffs need not allege such compensation was unreasonable because the section 408(b)(2) exemption is an affirmative defense. *Braden v. Wal-Mart Stores, Inc.*, 588 F.3d 585 (8th Cir. 2009).
  - Ninth Circuit: Embraced a "literal reading" of the statute without addressing whether the exemptions in section 408 are treated as affirmative defenses at the pleading stage. *Bugielski v. AT&T Services, Inc.*, 76 F.4th 894 (9th Cir. 2023).

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401(k) Plan Fees and Performance: Prohibited Transaction Claims *cont'd*

- Other circuits have characterized those decisions as "absurd" and have imposed additional pleading requirements:
  - Second Circuit: It is not enough to allege that a fiduciary caused the plan to compensate a service provider for its services. Instead, "the complaint must plausibly allege that the services were unnecessary or involved unreasonable compensation." *Cunningham v. Cornell Univ.*, 86 F.4th 961 (2d Cir. 2023).
  - Third Circuit: Plaintiffs must allege "an element of intent to benefit a party in interest." *Sweda v. Univ. of Penn.*, 923 F.3d 320 (3d Cir. 2019).
  - Seventh Circuit: The alleged transaction must "look[] like self-dealing," as opposed to "routine payments for plan services." *Albert v. Oshkosh Corp*., 47 F.4th 570 (7th Cir. 2022).
  - Tenth Circuit: "[S]ome prior relationship must exist between the fiduciary and the service provider to make the provider a party in interest under [section 406]." *Ramos v. Banner Health*, 1 F.4th 769 (10th Cir. 2021).

401(k) Plan Fees and Performance: BlackRock TDF Litigation

- Plaintiffs alleged that the BlackRock target date funds performed poorly relative to other target date funds and that in and of itself supported an inference on imprudence.
- Eleven copycat cases were filed by the same law firm in the summer of 2022.
- In an effort to shape the law in favor of plan sponsors and fiduciaries, American Benefits Council and others took the unusual step of submitting amicus briefs in support of motions to dismiss.

401(k) Plan Fees and Performance: BlackRock TDF Litigation *cont'd*

- Motion to dismiss rulings
  - Six cases were dismissed on motions to dismiss, with the courts finding:
    - Underperformance alone is insufficient to state a claim of imprudence,
    - The alleged underperformance was not serious or sustained enough, and/or
    - The alleged benchmarks were not meaningful due to material differences in strategy and objective.
  - One motion to dismiss was denied
    - Plaintiffs secured early discovery that enabled them to plausibly argue the existence of procedural errors, such as allegations that the plan fiduciaries violated the IPS, the committee did not meet quarterly, and meeting minutes did not reflect monitoring of the TDFs.
  - Four motions to dismiss amended complaints are pending.

401(k) Plan Fees and Performance: Recent Trials

- A jury verdict found that Yale University fiduciaries were not liable to plan participants for mismanaging their retirement plan. *Vellali v. Yale Univ.* (D. Conn. 2023), cross appeals pending.
  - The jury concluded that defendants breached their fiduciary duties by allowing unreasonable recordkeeping and administrative fees to be charged to participants, but nevertheless concluded that prudent decisionmaking *could* have created the same result.
- A bench trial judgment in favor of Aon Hewitt Investment Consulting. *Reetz v. Aon Hewitt Inv. Consulting, Inc.*, 74 F.4th 171 (4th Cir. 2023).
  - While AHIC had a conflict of interest in recommending proprietary funds, it acted as if it were free of any conflict because its self-interest did not motivate its advice. Its advice was "evenhanded" and included recommending passively managed funds which likely would have reduced the fees it received.
- A bench trial judgment in favor of Braun Medical. *Nunez v. B. Braun Med., Inc.*, 2023 WL 5339620 (E.D. Pa. Aug. 18, 2023).
  - The plan fiduciaries employed a robust process for managing the plan, including regular fiduciary meetings, hiring advisors, using watch lists to scrutinize underperforming funds, and negotiating lower recordkeeping fees. Furthermore, the investment performance and recordkeeping expenses were objectively reasonable.

401(k) Plan Fees and Performance: DOL Amicus Positions

Case Name	DOL Position
Pizarro v. Home Depot (11th Cir.)	A burden-shifting framework should have been applied such that once a fiduciary breach was demonstrated, defendants were required to disprove that the breach caused losses.
Vellali v. Yale (2d Cir.)	A burden-shifting framework should have been applied such that once a fiduciary breach was demonstrated, defendants were required to disprove that the breach caused losses.
Markham v. Variable Life Ann. (5th Cir.)	Prohibited transaction rules apply generally to service providers, not just plan sponsor insiders.
Parker v. Tenneco (6th Cir.)	Arbitration agreements cannot prospectively waive participant claims under ERISA section 502(a)(2).

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Actuarial Assumption Litigation

- The complaints have alleged that:
  - Plans use dated mortality assumptions (or fixed factors based on dated mortality assumptions) to calculate optional forms of benefits, including joint and survivor annuities.
  - Dated mortality assumptions assume a shorter life expectancy relative to updated mortality assumptions.
  - By assuming a shorter life expectancy, resulting benefit calculations are lower than they otherwise would be.

Actuarial Assumption Litigation *cont'd*

- Motion to Dismiss Rulings
  - Most motions to dismiss have been denied, with majority of courts finding that there is requirement for actuarial assumptions to be reasonable. *See, e.g.*, *Cruz v. Raytheon*, 435 F. Supp. 3d 350 (D. Mass. 2020).
  - Two courts granted motions to dismiss by ruling, contrary to most district courts, that there is no reasonableness requirement at all for mortality assumptions. *Reichert v. Kellogg*, No. 23-cv-12343 (E.D. Mich. Apr. 17, 2024); *Belknap v. Partners Healthcare*, 588 F. Supp. 3d 161 (D. Mass. 2022).
  - Some motions to dismiss have been granted on procedural grounds, *e.g.*, in favor of arbitration or administrative exhaustion (Eleventh Circuit only). *Duke v. Luxottica*, 2023 WL 6385389 (E.D.N.Y. Sept. 30, 2023) (compelling arbitration); *Brown v. UPS*, No. 20-cv-00460 (N.D. Ga. Aug. 27, 2020) (failure to exhaust administrative remedies).

Actuarial Assumption Litigation *cont'd*

- Potential Defenses
  - ERISA does not require or forbid the use of particular assumptions
  - Only certain forms of benefits are protected
  - Assumptions are reasonable if within reasonable range or when taking into account purpose of assumptions
  - Changing the assumptions will harm some participants
  - Statute of limitations

Claims to Watch

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Health Plan Claims

- The theories and claims advanced in lawsuits targeting 401(k) plan fees are being expanded to health plans.
- The new claims are attributable, at least, in part, to the DOL's expansion of the section 408(b)(2) regulations.
  - Since 2012, the regulations have required the disclosure of fees charged in connection with retirement plans.
  - More recently, the regulations require health plan brokers and consultants expecting $1,000 or more in direct and indirect compensation for services provided to group health plans to make detailed disclosures to the "responsible plan fiduciary" regarding their services and compensation.
    - The disclosure requirement applies to contracts and arrangements entered into, extended, or renewed after December 27, 2021.

Health Plan Claims *cont'd*

- Brokerage services may relate to, for example:
  - Selection of insurance products
  - Recordkeeping services
  - Medical management vendors
  - Benefits administration
  - Stop-loss insurance
  - Pharmacy benefit management (PBM) services
- It may be appropriate to request confirmation of compensation even if the service provider is not a covered broker or consultant.

Health Plan Claims *cont'd*

- A plan sued its third-party administrator alleging that it wrongfully paid providers' claims, retained undisclosed fees, and engaged in claims processing-related misconduct.

- Plan participants sued the plan fiduciaries alleged that their premium rates and cost-sharing (deductibles, copays, etc.) were too high because of commissions paid to plan's insurance broker.

- Plan participant sued the plan fiduciaries challenged costs paid for prescription drug benefits.

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Health Plan Claims *cont'd*

- Best Practices
  - Plan fiduciaries have a duty to monitor service providers, including pharmacy benefit managers and third-party administrators.
  - Request that service providers disclose all revenue received in connection with providing services to plan. Demand receipt of required disclosures.
  - When considering potential service providers, fiduciaries should compare their services, experience, fees and expenses, customer references, and other information relating to the quality of services.
  - ERISA does not require that plan fiduciaries always use the lowest cost vendor.
  - Consider whether to retain expert to provide monitoring assistance.
  - Consider conducting audits of claims processing.

Pension Risk Transfers

- ERISA permits plan sponsors to sell their pension liabilities to insurers. This is known as "derisking" or "annuitization."
- While the decision to annuitize is a settlor decision, the selection of an annuity provider is a fiduciary act.
- DOL Interpretive Bulletin 95-1 provides fiduciary standards for selecting an insurance provider, including but not limited to:
  - The quality and diversification of the annuity provider's investment portfolio;
  - The size of the insurer relative to the proposed contract;
  - The level of the insurer's capital and surplus;
  - The lines of business of the annuity provider and other indications of an insurer's exposure to liability;
  - The structure of the annuity contract and guarantees supporting the annuities, such as the use of separate accounts; and
  - The availability of additional protection through state guaranty associations and the extent of their guarantees.

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Pension Risk Transfers *cont'd*

- Lawsuits have been filed against three companies and, in some cases the independent fiduciary that approved the selection of the annuity provider, alleging that they violated ERISA by offloading pension obligations to an insurance provider connected to a private equity fund.
  - Plaintiffs allege that the defendants selected an annuity provider that was not the safest available because of its connection with private equity interests.
  - Plaintiffs claim this choice was made to save the defendants money instead of for the purpose of serving participants.
  - It is reasonable to anticipate that other such lawsuits will be filed, since many plans have entered into similar contractual arrangements with the same annuity company.
- Potential defenses include lack of standing, statute of limitations, reliance on an independent fiduciary, and the decision was prudent.

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