PROSKAUER ROSE LLP®

Client
Alert

A report
for clients
and friends
of the firm

September 2006

New Breed of ERISA Class Action Lawsuits

A series of copycat lawsuits against seven large companies and their 401(k) plan fiduciaries have been filed recently. Although it may be too soon to tell for certain, the seven complaints filed may be just the tip of the iceberg. The claims — all filed by the same law firm — generally challenge the methods by which fees are paid in connection with plan investments. The allegations focus primarily on "revenue sharing," which plaintiffs define as the transfer of asset-based compensation from brokers or investment management providers (such as mutual funds, common collective trusts, general insurance contracts, and similar pooled investment vehicles) to administrative service providers such as record-keepers, administrators and trustees in connection with 401(k) and other defined contribution plans. The compensation allegedly consists of monetary and non-monetary transfers such as credits for services, equipment, educational materials, conferences, meetings or seminars at luxury resorts. Plaintiffs contend that these revenue sharing arrangements, which they contend are common in the investment industry, are insufficiently scrutinized and/or described and thus violate various provisions under the Employee Retirement Income Security Act of 1974, as amended ("ERISA").

In addition to their "revenue sharing" claims, plaintiffs — in broad-brush fashion — also attack the validity of fees paid for a variety of plan services, including trustee, record keeping, administration, investment advisory, investment management, brokerage, insurance, consulting, accounting, legal, printing, mailing, and other services. The complaints also attack investments in employer stock, albeit for different reasons than those asserted in the "stock drop" cases of the recent past. The new attacks on the employer stock funds are two-fold: that plan fiduciaries violated ERISA by charging excessive fees and expenses to the company stock fund, and that the fiduciaries breached their obligations by maintaining cash in a unitized company stock fund, causing participants to realize less of a gain when the employer's stock price rose.

In connection with their claims, plaintiffs allege that the plan fiduciaries breached their duties under ERISA by: (1) permitting the plans to pay excessive and unreasonable fees and expenses through "hard dollar" and "revenue sharing" payments; (2) failing to monitor the fees and expenses paid by the plans; (3) failing to discover, disclose and stop hidden and excessive fees charged to the plans; (4) failing to know industry trends, developments, practices and policies in the retirement, financial investment and securities industries that affect plans; (5) failing to understand the method by which plan vendors collect revenue from plans; (6) failing to establish, implement, and follow procedures to properly and prudently determine whether the fees and expenses paid by the plans were reasonable and incurred solely for the benefit of participants; (7) failing to disclose the total fees and expenses to plan participants; and (8) failing to clearly communicate to participants about the transactions, fees and expenses that affect their account balances.

Plaintiffs also contend that because the companies did not fully disclose the fees and expenses to plan participants, they cannot rely on the safe harbor provisions of ERISA § 404(c) to shield them from liability. ERISA § 404(c) insulates fiduciaries from liability for participant losses in a plan to the extent that the participant controls the assets in his or her account.

There is reason to be concerned that these lawsuits will proliferate. We have information indicating that the law firm that filed the seven complaints two weeks ago also has sent detailed requests to other large employers seeking a host of plan-related information including plan documents, summary plan descriptions, trust agreements, and annual reports. The requests also have sought detailed information about the underlying assets or investments for each investment fund in the plan; wrap fees, expense ratios and yields for the plans' investment funds; revenue sharing agreements with service providers; and the identification of all service providers (including pension consultants, investment managers, record keepers, brokers, administrators, and trustees) and the amount of compensation paid to each.

Whether or not the claims asserted proliferate, they do serve to underscore the significance of procedural prudence in all aspects of plan investments and plan administration. While there may be many procedural and legal defenses to the claims asserted, the surest defense is a clear record reflecting that all the issues raised by these claims were contemporaneously considered, investigated, vetted and addressed.

NEW YORK • LOS ANGELES • WASHINGTON

BOSTON • BOCA RATON • NEWARK

NEW ORLEANS • PARIS

Client Alert

Proskauer Rose's Employee Benefits Litigation Group is a significant and rapidly-growing component of the Firm's nationally-renowned Labor and Employment Law Department. With nearly 30 litigators nationwide, backed by an additional 25 substantive ERISA practitioners, our team handles the full gamut of litigation matters facing employee benefits practitioners.

New York

Myron D. Rumeld
212.969.3021 – mrumeld@proskauer.com

New Orleans

Howard Shapiro
504.310.4085 – howshapiro@proskauer.com

Robert W. Rachal
504.310.4081 – rrachal@proskauer.com

Newark

Amy Covert
973.274.3258 – acovert@proskauer.com

Proskauer Rose is an international law firm that handles a full spectrum of legal issues worldwide.

You can also visit our Website at **www.proskauer.com**