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Massachusetts District Court Permits 403(b) Plan Fiduciary Breach Claims to Proceed

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A federal district court in Massachusetts recently denied a motion to dismiss a complaint filed by plan participants in the Cape Cod Healthcare, Inc. 403(b) plan, which alleged that the plan's fiduciaries breached their ERISA duty of prudence by permitting the plan to pay excessive recordkeeping fees and remain invested in overpriced, underperforming investment options. *Somers v. Cape Cod Healthcare, Inc.*, No. 23-cv-12946 (D. Mass. Aug. 30, 2024).

Plaintiffs, both former employees of Cape Cod Healthcare, alleged that Cape Cod Healthcare (plan sponsor and named fiduciary) and individual fiduciary defendants breached their fiduciary duty in two ways.

First, plaintiffs alleged that the plan's recordkeeping fees of approximately $71 per-participant were excessive. To support this claim, plaintiffs compared the plan's per-participant fees to the average recordkeeping fee allegedly paid by similarly-sized defined contribution plans, as reported by NEPC, a consulting group that surveyed such plans. Plaintiffs also alleged that the $71 figure likely underreports the per-participant recordkeeping fees, because it did not include revenue sharing payments made to the recordkeeper.

Second, plaintiffs challenged the plan's retention of three investment options. Plaintiffs contended that two of the challenged investments charged excessive fees and underperformed, based on comparisons to allegedly comparable funds. For one of the challenged investments, the complaint failed to explain why the proposed comparators were similar in kind, and the complaint alleged that the second investment was similar to its proposed comparators because the funds are in the same Morningstar category.

The third challenged investment was a stable value fund affiliated with Lincoln Financial. Plaintiffs alleged that its guaranteed minimum interest rate and portfolio rate were "far below the rate of inflation," as well as the rates for the stable value fund in Lincoln Financial's own retirement plan.

In denying defendants' motion to dismiss, the court first rejected defendants' argument that plaintiffs lacked standing because they did not allege that they invested in any of the challenged investment options. In so holding, the court explained that "it is well-established that for the purpose of constitutional standing, a plaintiff need not have invested in each fund at issue, but must merely plead an injury implicating defendants' fund management practices," and plaintiffs had done so by alleging that defendants failed to ensure that the plan paid reasonable fees and maintained appropriate investment options.

The court also rejected defendants' arguments that the complaint failed to state viable claims. In permitting the recordkeeping fee claim to proceed, the court declined to entertain defendants' arguments that plaintiffs miscalculated the per-participant's recordkeeping fees, and that the NEPC survey did not present a meaningful comparison because it says nothing about the services provided by recordkeepers to the plans at issue – a position that several other district courts, and at least one Circuit Court, have agreed with. According to the court, these arguments required a factual analysis that is inappropriate for the pleadings stage. For similar reasons, the court declined to consider defendants' arguments regarding the plan's investment options, including that: (i) plaintiffs did not establish that their alleged alternative investments were "meaningful benchmarks"; and (ii) the complaint itself showed that two of the challenged investments performed on par with or outperformed plaintiffs' alternative investments over the relevant period. Instead, the court was persuaded by allegations that defendants did not remove any of the challenged investments during the relevant time period; there were several "superior alternative options . . . available on the market"; and the guaranteed minimum interest rate and portfolio rate of the plan's SVF were less than those in the SVF offered by the comparator plan.

Proskauer's Perspective

This decision is an eye-opening illustration of how, without universally-accepted pleading standards for claims of this nature, the outcome may turn on the proclivities of the court. Specifically, the court's holding that plaintiffs had standing, despite not alleging that they invested in *any* of the challenged investments, is at odds with other district court decisions finding that plaintiffs lacked standing under similar circumstances. Furthermore, the court's refusal to consider the argument that plaintiffs failed to identify "meaningful benchmarks" in support of their recordkeeping and investment claims adds a decision to the column of those courts that have ruled similarly, on the ground that this is a factual issue. But it is contrary to the established pleading standard in multiple Circuit Courts and that has been applied by a growing number of district courts, including one within the same District.

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