

## **CLASS ACTION SUIT TARGET RETIREMENT PLAN FEES**

According to estimates, the “hidden” costs related to 401(k) plan investment fees and their impact on investment performance are significant – \$25 billion annually. For plan fiduciaries, these amounts serve to underscore the necessity of comprehensively understanding the true cost of plan administration. The Employment Retirement Income Security Act (“ERISA”) requires retirement plan fiduciaries to act solely in the interests of plan participants and beneficiaries, and with “the care, skill, prudence and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use.” This includes a responsibility to assure that plan fees and costs are “reasonable” and that participants receive adequate and appropriate information to aid in selecting among available investment alternatives.

Several class-action lawsuits have heightened awareness of plan fees and have raised the question of potential fiduciary liability related to such fees. Since last fall, the St. Louis, Missouri law firm Schlichter, Bogard & Denton has filed more than ten class action suits against large corporate plan sponsors alleging various breaches of fiduciary duties and seeking restitution for excess fees. While the details of the complaints filed in the cases vary, the alleged breaches relate to excess fees, improper or incomplete disclosures of fees, and improper oversight of plan expenses.

A central theme in all of the complaints is the industry usage of revenue sharing arrangements and 12b-1 fees. “Revenue sharing” encompasses many types of fee sharing arrangements, but it can be broadly defined as the transfer of a portion of the asset-based investment management fees charged by mutual funds to plan service providers. 12b-1 fees refer

to fees charged on some mutual fund shares that are intended to be used to market the fund. The complaints allege that fiduciaries have violated their ERISA obligations by failing to appropriately investigate and evaluate revenue sharing arrangements when negotiating with services providers and that the resulting total cost to participants is unreasonable. In addition, the plaintiffs claim that the failure to disclose the exact details of the fee arrangements is a breach of the sponsor's duties of disclosure under ERISA.

The complaints also assert that plan sponsors have failed to appropriately manage certain aspects of the plan as the plan assets grow. Over time, asset-based fees can dramatically increase and, the complaints allege, result in excessive charges. Plans may also become eligible for lower-cost mutual fund share classes as plan assets increase. The complaints allege that the fiduciaries' failure to monitor these charges and negotiate changes in share classes resulted in excessive fees.

Finally, the complaints focus on plans offering company stock funds alleging that participants suffered unreasonable losses because the company stock fund held excess cash and charged excessive investment management fees. The complaint alleges that the excess cash and excessive fees resulted in a lower rate of return than a non-plan investor would receive investing in company stock on the open market.

In response to the complaints, plan sponsor's have been relying in part on the protections provided under ERISA §404(c). ERISA §404(c) relieves plan fiduciaries from liability for individual participant investment decisions provided certain requirements are met. Plaintiff's, however, argue that plan fiduciaries are responsible for the prudent selection and management of the investment alternatives of the plan for which ERISA §404(c) provides no protection.

While the lawsuits are at an early stage and it is difficult to predict their outcome, they have already faced some opposition from the courts. One of the suits, *Hecker v. Deere & Company* was recently dismissed in the U.S. District Court, Western District of Wisconsin. The court decided Deere & Company's participant disclosures actually reflected the total expenses for fund management and met the existing reporting requirements. They also indicated that the Department of Labor's ongoing review of revenue sharing arrangements confirms the position that detailed disclosure of such arrangements is not presently required. Further, the variety of investment alternatives offered by Deere & Company's plan allow participants to evaluate the range of available expense ratios and exercise control over their investments thereby insulating Deere & Company from liability. Courts in other jurisdictions, however, have not followed this decision and have refused to dismiss the cases in the early stages of litigation.

Despite the outcome of these cases, the concerns raised by the current lawsuits will remain relevant. The transparency, reporting, and disclosure of various types of fee arrangements have been topics of debate for the Securities and Exchange Commission, the Department of Labor, Congressional hearings, and the New York Attorney General's office. Thus, plan sponsors must provide more transparency of plan fees and they must continue to help participants make the most of their retirement savings by leveraging plan assets and selecting investment options that balance performance with expense. In particular plan sponsors should:

- Review all plan services agreements, including administrative and investment fee arrangements.
- Require all plan vendors to disclose revenue sharing arrangements.
- Review the current disclosures to plan participants and modify as necessary to clarify charges for plan expenses.

- Review the plan's investment policy statement and assure that the plan investment alternatives comport with such policy.
- If the plan includes a company stock fund, review the expenses related to the fund and the amount of cash reserves held in the fund.
- Have a review of the plan conducted by an independent consultant who can assist with evaluating, and suggest possible changes to the plan's administration, investment options, and participant disclosures.
- Obtain fiduciary insurance to protect plan fiduciaries from the expense of suits and possible exposure to liability.

Nearly 50 million U.S. workers have a 401(k) account, thus the emphasis on prudent plan management is here to stay. Whether the current litigation has merit under ERISA remains to be seen, but it is critical that plan fiduciaries implement an ongoing process enabling them to ensure that plan expenses are reasonable and plan investment alternatives meet ERISA's prudent investment standards.

*The Fiduciary Liability article in this issue was provided by Richard Hackett and John Nichols of Gray Plant Mooty. Drawing on over 140 years of experience, Gray Plant helps businesses move forward because it knows where business has been. Gray Plant's employee benefits and executive compensation group provides services to clients throughout the country. Gray Plant Mooty is headquartered in Minneapolis with offices in St. Cloud, Minnesota and Washington, DC. Gray Plant is an affiliate of MULTILAW and the Employment Law Alliance, and its 160 attorneys serve regional, national, and international clients in all areas of law. For more information about Gray Plant Mooty, visit [www.gpmlaw.com](http://www.gpmlaw.com).*