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ERISA Fee Litigation: Overview of Developments in 2012 and What to Expect in 2013

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Introduction

Traditional defined benefit pension plans have been or are being phased out, and American workers must rely even more on their savings in participant-directed plans, such as tax code Section 401(k) plans, to fund their retirements. Given this shift, and in the aftermath of the global financial crisis affecting savings values, the fees collected from and profits generated by 401(k) plans matter. Approximately $3 trillion in assets sit in participant-directed plans with an estimated 72 million participants.[1] According to the Department of Labor, just a 1 percent difference in fees over an investment lifetime—*i.e.*, the difference between an expense ratio of 0.50 percent (50 basis points[2]) and 1.50 percent (150 basis points)—reduces retirement savings by *more than a quarter*.[3] Because this impact on plan participants is so clear, a number of the retirement services industry's longstanding practices are being challenged by astute participants and plan fiduciaries, many of whom have taken to court those who collect fees and profit from their relationships with plans that are governed by the Employee Retirement Income Security Act.

This report begins with a description of the conduct that fee litigation targets and who the parties are in fee cases, followed by a summary of the 2012-2013 litigation landscape. It then provides details and perspective on a number of significant fee litigation outcomes that have emerged in the past year or so. The report then turns to a discussion of pending cases and what to watch in 2013 in this dynamic segment of ERISA jurisprudence and practice.

Conduct Targeted by Fee Litigation

ERISA fee litigation has been prevalent since 2006.[4] Filings of new cases were heavy from 2006 through 2008, and picked up again from 2010 through 2012. These cases challenge fees that are paid by participants out of plan assets in defined contribution plans and/or collected by 401(k) plan service providers. Thus, fee litigation targets both *direct* fees—collected by service providers from participants and plans—and *indirect* fees—typically collected by service providers from other service providers or from mutual fund companies. Indirect fees—often hidden or opaque in their design and disclosure—drive overcompensation of service providers and result in failures to keep direct fees as low as

[1] *See* U.S. Dep't of Labor, Emp. Benefits Sec. Admin., Fact Sheet, Final Rule to Improve Transparency of Fees and Expenses to Workers in 401(k)-Type Retirement Plans 1 (Feb. 2012), *available at* http://www.dol.gov/ebsa/newsroom/fsparticipantfeerule.html.

[2] One basis point is equal to 1/100th of 1 percent and is the method commonly used to express investment returns and expenses. For example, fifty basis points equal 0.50 percent.

[3] U.S. Dep't of Labor, Emp. Benefits Sec. Admin., *A Look at 401(k) Plan Fees* 2 (Oct. 2010), *available at* http://www.dol.gov/ebsa/publications/401k_employee.html.

[4] One of the earliest-filed cases bearing on fiduciary status in excessive fee litigation, *Haddock v. Nationwide*, No. 01-1552 (D. Conn.), was filed in 2001, with influential rulings emerging in 2006. *See Haddock v. Nationwide Fin. Servs. Inc.*, 419 F. Supp. 2d 156, 36 EBC 2953 (D. Conn. 2006).

they could be in a world where the whole fee picture is apparent to decisionmakers. Conflicts of interest too may keep fees high, particularly when fiduciaries or service providers include their own proprietary investment products in the 401(k) plans they run.[5]

Three core types of conduct are at issue in current ERISA fee litigation:

- Collection of excessive or unreasonable fees or kickbacks, regardless of disclosure. Key markers of such claims are imprudent or self-interested selections—*e.g.*, unbenchmarked, underperforming, expensive investment options with 12b-1, sub-TA,[6] and other fees, excessive or unchecked revenue sharing, and/or other unnecessary or uncalculated (and thus unmonitored) fees.

- Collection of hidden fees, which includes charges of any kind that service providers and/or fiduciaries choose not to itemize or communicate to decisionmaking fiduciaries or to participants.

- Collection of self-determined fees, which involves the height of self-dealing through control over plan assets, because the ability to control one's own compensation confers fiduciary status and easily leads to ERISA violations.

For all of these fact patterns, complaints that allege conflicts of interest, kickbacks, self-dealing, and the collection of undisclosed fees give rise to the most successful cases, because these practices provide the breach-of-loyalty and prohibited transaction hooks that the courts find most compelling. Concealment of fees all but ensures an ERISA fiduciary breach or prohibited transaction claim and has a rippling impact because fiduciary decisionmakers lack the critical information to assess fee reasonableness that they need to comply with their fiduciary duties. Finally, benchmarking—*i.e.*, comparing investment options and fee structures to other available alternatives—remains a vital part of prudence evaluations. Failure to benchmark or to ask for discounts, deals, rebates, or lower share classes can spell liability. Fiduciaries must monetize fee structures and know both *how* and *how much* service providers are being paid. Costly investment option selections are actionable, but plaintiffs must allege more than the mere availability of other options or a menu that is simply too small. Instead, plaintiffs must allege some benchmarking deficiency, an imprudent selection process, fiduciary self-dealing, or the presence of kickbacks in order to plead a case that will withstand the typical defenses.

[5] *See* Veronika Pool, Clemens Sialm, & Irina Stefanescu, *It Pays to Set the Menu: Mutual Fund Investment Options in 401(k) Plans*, Netspar Discussion Papers (Jan. 20, 2013).

[6] Sub-TA fees—also known as "subtransfer agent" fees—are fees paid by mutual funds to plan investment option platform fiduciaries or recordkeeping service providers. They are often calculated on a per-participant basis and may be completely out of view to plan fiduciaries and participants.

The Parties

A legal challenge to fees and fee structures can come from plan fiduciaries or participants,[7] and will put fiduciary decisionmakers who turn a blind eye to fees or fail to investigate them on the hot seat, regardless of their affiliation. As the cases discussed below demonstrate, both plan sponsor-affiliated plaintiffs and participant plaintiffs have been pushing fee litigation forward to recover losses to their plans and to seek disgorgement of ill-gotten gains caused by the ERISA violations of both fiduciary and non-fiduciary entities.

Some cases are focused on a single plan or group of plans affiliated with a single employer and are pled as a class of participants. Others are broader: "class of plans" cases target the conduct of fiduciary and non-fiduciary service providers whose common practices reach across hundreds or thousands of plans. All varieties have met with success at different procedural milestones, and plaintiffs continue to file fee cases.

Fee Litigation Landscape, 2012-2013

With several years of foundational case law on the books demonstrating the importance of a prudent process[8] and the consequences of service provider discretion over fees,[9] ERISA fee jurisprudence continues to evolve. Outcomes in 2012—in motions practice, trial, and settlements—indicate the continued importance of a prudent process that rigorously assesses fee reasonableness through benchmarking. The appropriate (or inappropriate) wielding of power is an important theme in 2012's case law. Courts are *requiring* the use of plan bargaining power to keep fees low and they have taken fiduciaries to task for the converse—using control over plan assets to benefit themselves or their corporate interests.

The emerging case law also confirms ongoing liability risks arising out of conflicts of interest, kickbacks, self-dealing, and undisclosed fees for both plan fiduciaries and non-fiduciary service providers. With the Department of Labor's fee disclosure rules now in place—requiring increased information flow from service providers to plan fiduciaries,[10] and from plan sponsors to participants[11]—a lot of new information about fees is ostensibly becoming available to would-be fee litigants. In particular, revelations about fees that were previously hidden and now have been disclosed for the first

[7] *See* ERISA § 502(a)(2), 29 U.S.C. § 1132(a)(2), and ERISA § 502(a)(3), 29 U.S.C. § 1132(a)(3) (both allowing a civil action for violations of ERISA to be brought by a "participant, beneficiary, or fiduciary").

[8] *E.g.*, *Braden v. Wal-Mart Stores*, 588 F.3d 585, 48 EBC 1097 (8th Cir. 2009).

[9] *E.g.*, *Charters v. John Hancock Life Ins. Co.*, 583 F. Supp. 2d 189, 45 EBC 1183 (D. Mass. 2008); *Haddock v. Nationwide Fin. Servs. Inc.*, 419 F. Supp. 2d 156, 36 EBC 2953 (D. Conn. 2006).

[10] *See* 29 CFR § 2550.408b-2 (the "408(b)(2) regulation," published in final form at 77 Fed. Reg. 5,632 (Feb. 3, 2012)).

[11] *See* 29 CFR § 2550.404a-5 (the "404(a) regulation," published in final form at 75 Fed. Reg. 64,910 (Oct. 20, 2010)).

time are likely to fuel more fee litigation, particularly against fiduciary service providers.[12]

This report covers the highlights from 2012, followed by early developments in 2013 and a preview of what more to expect in 2013 and beyond.

Highlights from 2012

Bench Trials: A Landmark Decision in *Tussey v. ABB*

Tussey v. ABB, Inc., No. 06-4305 (W.D. Mo.), is only the second of two excessive fee cases tried to the bench that resulted in a post-trial ruling.[13] The other was *Tibble v. Edison Int'l*, No. 07-5359 (C.D. Cal.), which was affirmed by the Ninth Circuit Court of Appeals.[14]

For plaintiffs, *Tussey* represents a sweeping win on multiple issues—one that is far more favorable than *Tibble* on the law and with a much more substantial award for losses to the plan. Compared to the summer 2010 award of $370,732 to the *Tibble* plaintiffs for the excessive fees on three mutual funds (which left the plaintiffs with more to appeal than defend), the $36.9 million post-trial win in *Tussey* is a landmark result.

Background

The four-week *Tussey* trial was held in January 2010. The trial followed a largely favorable summary judgment opinion for the plan participant plaintiffs on Dec. 7, 2009, and examined several important issues, which were resolved by Judge Nannette Laughrey's trial order more than two years later.

Tussey involved two retirement plans—one for ABB's union employees and the other for non-union employees. Defendant Fidelity Trust provided recordkeeping services to the plans and defendant Fidelity Research provided investment advice to the Fidelity mutual funds offered by the plans. The Fidelity entities also provided corporate services to ABB, including payroll and recordkeeping for ABB's health and welfare plans, as well as its defined benefit and highly compensated employee plans. As it turned out, ABB turned a blind eye to whether it received a "very favorable price for the work Fidelity did for ABB's corporate services," to the detriment of the plans (hereinafter, collectively, the "plan").[15]

Key Findings of Fact

Revenue Sharing. Fidelity Trust received recordkeeping compensation primarily through revenue sharing. Central to ABB's liability for failure to monitor recordkeeping fees was that ABB "never calculated the dollar amount of the recordkeeping fees" paid by the plan to Fidelity, "nor did it consider how the Plan's size could be leveraged to reduce recordkeeping costs."[16] ABB also failed to "obtain a benchmark" for what recordkeeping should have cost the plan, and failed to do so even when an outside consultant "told ABB that it was overpaying for recordkeeping and that it appeared that [the plans] were subsidizing the corporate service provided to ABB by Fidelity."[17]

The court found three factors important in ABB's failure to monitor the reasonableness of revenue sharing: (1) expense ratios alone do not reveal revenue sharing amounts; (2) expense ratios do not reveal the competitive market for recordkeeping fees; and (3) expense ratios fail to take into account the size of the plan, its bargaining heft, and the benefits of inclusion that flow to the chosen funds.

The court found that ABB was wrong to focus on per-participant flat fees and rejected its "progressivity" defense as both incongruent with the spread of actual participant investments (*i.e.*, high assets in the plan do not ensure high assets invested in funds that share revenue) and with the actual costs of administering the plan (*i.e.*, accounts with more money invested in actively managed funds do not translate into accounts that require more recordkeeping).

The court also rejected the defendants' "risk sharing" argument in support of revenue sharing, because a recordkeeper can simply demand more flat or per head fees to replace lost revenue sharing if assets decline in value. The court faulted ABB for never determining "how much revenue sharing was collected by Fidelity and, therefore, [ABB] did not and never was in a position to ask for a rebate when Fidelity revenue sharing exceeded the value of the recordkeeping services provided."[18]

Investment Policy Statement. In its findings of fact, the *Tussey* court found that ABB's failure to negotiate rebates ran afoul of the Investment Policy Statement's requirement that "at all times, [Alliance], rebates will be used to offset or reduce the cost of providing administrative services to plan participants."[19]

Fund Mapping. ABB replaced the Vanguard Wellington Fund with the Fidelity Freedom Funds. The mapping proposal that ABB considered ensured that flat recordkeeping fees would go down, and revenue sharing would go up. With the switch, ABB, Inc. would be able to reduce its own costs and also obfuscate the fact that employees were actually paying for the administration of the plan. Additionally, because of the opacity of revenue sharing as compared to flat fees, ABB retained the recruiting power of a plan that appeared to be low cost to employees.[20] Meanwhile, from 2001 to September 2005, "Fidelity received an additional 35 basis points as a result of the Freedom Funds being selected."[21] ABB

[12] *See* Gretchen S. Obrist, "ERISA Fee Litigation: The Impact of New Disclosure Rules, and What's Next in Pending Cases," Pension & Benefits Daily, Bloomberg BNA (Feb. 21, 2013).

[13] *Tussey v. ABB, Inc.*, No. 06-4305, 2012 BL 84927, 52 EBC 2826 (W.D. Mo. Mar. 31, 2012).

[14] *Tibble* is discussed *infra*.

[15] *Tussey*, No. 06-4305, 2012 BL 84927, 52 EBC 2826.

[16] *Id.*

[17] *Id.*

[18] *Id.*

[19] *Id.*

[20] *Id.*

[21] *Id.*

failed to calculate the cost to the plan of the change. To make matters worse, the removed Wellington Funds outperformed the Freedom Funds between 2000 and 2008.

Share Class Selection. ABB selected "share classes with higher expenses than other available share classes" for six funds "because of the investments' effect on ABB's method of compensation to Fidelity Trust," ignoring these selections' detriment to participants.[22]

Subsidizing Corporate Administrative Services with ERISA Plan Fees. In response to Fidelity's decision to increase per-participant fees to compensate for the loss of revenue sharing, ABB negotiated with Fidelity over a new compensation arrangement. In the process, ABB considered not just plan-related expenses, but also a plethora of corporate costs that were paid to Fidelity. Not only did ABB fail to keep these spheres of revenue to Fidelity separate, it ignored an outside consultant opinion that ABB "overpaid for Plan recordkeeping services and that the Plan's recordkeeping payments via revenue sharing appeared to be subsidizing services for ABB corporate plans."[23]

Float. Interest income generated on funds sitting in accounts used to facilitate various plan transactions was kept by Fidelity and/or distributed to mutual fund shareholders outside the plan. The court found that this compensation was above and beyond what Fidelity was entitled to receive under the Trust Agreement and that funds were not solely used to benefit plan participants.

Resolution of Legal Claims and Remedies

First, the *Tussey* court found the ABB plan sponsor defendants liable for failure to monitor recordkeeping costs, as well as failure to negotiate rebates for the plan from the plan recordkeeper (Fidelity Trust), from the mutual fund adviser to Fidelity funds in the plan (Fidelity Research), or from other investment companies chosen to be in the plan investment lineup. The ABB defendants were found to have breached their fiduciary duties as well by selecting "more expensive share classes" for the plan lineup "when less expensive share classes were available" and committing ERISA Section 406(a) prohibited transactions for removing a Vanguard fund and replacing it with Fidelity funds.[24] Based on the expert analysis submitted by the plaintiffs, the court found that failure to monitor recordkeeping costs and negotiate for rebates resulted in losses of $13.4 million to the plan. Further, based on the expert analysis submitted by the plaintiffs, the court found that improper mapping caused losses of $21.8 million to the plan. While the court found that plaintiffs' expert was credible as to share class selection and that the plan suffered losses, the court found that such damages are subsumed in the damages it awarded for excess recordkeeping fees. The ABB defendants have joint and several liability for these losses.

[22] *Id.*
[23] *Id.*
[24] *Id.*

Second, ABB, Inc. and the company's benefits committee violated their fiduciary duties of loyalty when they "agreed to pay Fidelity an amount that exceeded market costs for Plan services in order to subsidize the corporate services provided to ABB by Fidelity" (payroll, recordkeeping for health and welfare plan and defined benefit plan).[25] The court found the self-dealing damages already accounted for by the award for excess recordkeeping fees.

As for Fidelity, the *Tussey* court found that Fidelity breached its fiduciary duties of loyalty to the plan when it "failed to distribute float income solely for the interest of the Plan" and that Fidelity Research breached its fiduciary duties when it "transferred float income to the Plan's investment options instead of the Plan."[26] The court awarded $1.7 million for losses due to mishandling of float with joint and several liability for the Fidelity defendants.

ERISA Section 406(b) prohibited transaction claims against Fidelity Trust associated with the Vanguard-to-Wellington map failed, because Fidelity Trust did not know that "some options would effectively transfer recordkeeping fees from ABB, Inc., to the Plan."[27] Fidelity Trust also escaped liability as a co-fiduciary because it did not have "veto" power.

The court rejected the plaintiffs' claim that more comingled funds or separate accounts should have been used in lieu of mutual funds, because this decision was not arrived at imprudently and did not violate the Investment Policy Statement.

As described above, the court ordered compensation to the Plan for losses and ill-gotten gains when the defendants "used Plan assets for their own benefit."[28] The court also ordered injunctive relief, including a competitive bidding process with request for proposals for a new recordkeeper within 18 months, monitoring of recordkeeping fees, dollar amount calculations to determine the exact fees paid to the recordkeeper, and leveraging of its size to negotiate for rebates. The court also prohibited use of the same recordkeeper for ERISA plan and nonplan related services and required ABB to choose the lowest share classes. Fidelity was ordered not to transfer float to any entity other than the plan, participants, or beneficiaries, "unless expressly permitted" by its agreements with the plan.[29]

Lessons from Tussey

The opinion articulates the following standards for evaluating prudence, loyalty, and prohibited transactions:

- **Revenue Sharing.** Revenue sharing is not *per se* imprudent. To assess the prudence of revenue sharing arrangements, benchmarking is a must. Without a baseline, it is "impossible" to determine whether both rev-

[25] *Id.*
[26] *Id.*
[27] *Id.*
[28] *Id.*
[29] *Id.*

enue sharing arrangements and the fees as a whole (including any per participant or other fees) are, holistically, a good value to the plan. The context of the particular plan at issue matters. Examination of expense ratios alone is not enough. The fact that others in the industry use a particular method is not justification enough. Fee structures must "offset or reduce" costs vis-a-vis other available methods.

- **Fund Mapping.** In mapping, a "winnowing process" is a necessary part of the gatekeeping function of fiduciaries. Underperforming, overpriced funds are imprudent. Investment Policy Statement guidelines for benchmarking, evaluation, and "watch list" treatment are important—failing to adhere to them is a red flag, particularly when the contemplated move will benefit the *plan sponsor* (here an ERISA "party in interest") instead of the plan.
- **Share Class Selection.** Choosing more expensive share classes instead of lower-cost options is imprudent. Justifying higher-cost fund selections based on "revenue neutral" revenue sharing income requirements that themselves resulted from prohibited transactions (here the mapping of Wellington Funds to the Freedom Funds) is not allowed. Ignoring an Investment Policy Statement requiring the lowest share classes for a given investment is imprudent.
- **Self-Dealing.** It is a violation of ERISA's duty of loyalty to subsidize corporate costs with an ERISA plan. Fiduciaries who tether ERISA plan fee negotiations to non-ERISA plan services will face liability for fiduciary breach and prohibited transactions.
- **Float.** It is a violation of ERISA's duty of loyalty for a fiduciary to retain and/or distribute outside the plan float income.

Tussey demonstrates that self-dealing and adherence to the duty of loyalty are paramount in identifying claims that will be successful and result in an award of losses to a plan. Fiduciaries with bargaining power must use it for the benefit of the plan, not themselves or their corporate interests.

Attorneys' Fees and Costs

On Nov. 2, 2012, the U.S. District Court for the Western District of Missouri awarded $12.9 million in attorneys' fees and approximately $490,000 in costs to be paid jointly and severally by all defendants. The court also awarded $1.7 million in costs to be paid out of the class damages award and $25,000 from the class award to each of the three named plaintiffs.[30] Thus, the defendants' total court-ordered liability exceeds $50 million.

Defendants' Appeal to the Eighth Circuit

Defendants appealed to the U.S. Court of Appeals for the Eighth Circuit (No. 12-2056). Opening briefs are due April 29, 2013, and several *amici* already have appeared. Depending on how quickly the briefing schedule progresses, a ruling could be issued by the Eighth Circuit before the end of 2013.

[30] *Tussey v. ABB, Inc.*, No. 06-4305, 2012 BL 288894 (W.D. Mo. Nov. 2, 2012) (ECF No. 718).

Plausible Claims: *Krueger v. Ameriprise* Pushes the Law Forward

By now it is clear that ERISA fee cases involve quintessentially *process*-based claims.[31] The *Braden* court found it *critically important* that ERISA plaintiffs have no access to key facts such as specific details about the fund selection process or other "inside information."[32] Instead, such plaintiffs merely have facts about the results of the process. Accordingly, the remedial scheme of ERISA mandates that such plaintiffs' allegations be afforded "careful and holistic" consideration.[33] *Krueger v. Ameriprise Fin., Inc.*[34] adheres to these principles absolutely.

Facts

The core factual allegations in *Krueger* are that Ameriprise Financial, Inc. orchestrated the investment of hundreds of millions of dollars into investment products operated by Ameriprise, its subsidiaries, and Wachovia (which purchased Ameriprise's recordkeeping business and provides recordkeeping to the plan). The swelling of assets in its own products made them more marketable to the outside world. Plaintiffs—participants in the plan—alleged poor performance and multiple layers of excessive fees charged to participants, profiting Ameriprise at the expense of the plan.

Fee Claim Analysis

Prudence and Loyalty. Judge Susan Richard Nelson's opinion in *Krueger* cited *Braden* at length in its legal standard and ERISA Section 404 breach analysis, as well as relied on *Gipson v. Wells Fargo & Co.*[35] The court in *Krueger* easily found it plausible that defendants' process was flawed and that self-interest tainted investment selection, based on Ameriprise's use of plan assets to "seed new and untested affiliated mutual funds" and its choice of investment options with "poor or non-existent performance histories relative to other investment options that were available."[36] *Krueger* rejected the defendants' attempt to distinguish *Braden* on the facts (no "static" lineup, no 12b-1 fees, no revenue sharing kickbacks to the trustee), finding that the point was that a plaintiff needs to allege flawed evaluation and choosing poorly. Thus, not only can many different factual scenarios present a viable case, *Krueger* reinforces *Braden*'s holding that "specific facts" need not be pleaded.

[31] *Braden v. Wal-Mart Stores, Inc.*, 588 F.3d 585, 595, 48 EBC 1097 (8th Cir. 2009) ("In evaluating whether a fiduciary has acted prudently, we . . . focus on the process by which it makes its decisions rather than the results of those decisions.").

[32] *Id.* at 598.

[33] *Id.*

[34] *Krueger v. Ameriprise Fin., Inc.*, No. 11-2781, 2012 BL 313619 (D. Minn. Nov. 20, 2012).

[35] *Gipson v. Wells Fargo & Co.*, No. 08-4546, 46 EBC 1391 (D. Minn. Mar. 13, 2009).

[36] *Krueger*, No. 11-02781, 2012 BL 313619.

Notably, *Krueger* also rejected the defendants' reliance on the three-judge panel opinion *Hecker v. Deere & Co.*,[37] and *Renfro v. Unisys Corp.*[38] *Krueger* cited the *en banc* ruling in *Hecker*, which clarified that *Hecker I* "was tethered closely to the facts before the court."[39] Distinguishing *Hecker* and *Renfro*, the court in *Krueger* emphasized that the *Krueger* plaintiffs alleged a tainted process and self-interested decisionmaking, not just the presence of retail funds or potentially lower fees.

More significantly, the court squarely rejected the idea—advanced widely by defendants in fee litigation—that a large variety of investment options undermines a plaintiff's claim. The Ameriprise plan had *900 options*, only a fraction of which appeared to be affiliated funds (though convoluted transfer rules seem to have provided extra fees associated with all of the options, helping to establish the self-dealing needed to make a good case). *Krueger* relied on *Pfeil v. State Street Bank & Trust Co.*[40] and *DiFelice v. U.S. Airways*[41] to make the point that just one bad option can pollute an otherwise good lineup and variety cannot "inoculate" a fiduciary from liability.[42] This approach belies the idea that brokerage windows and large swaths of investment options are a panacea for defendants.

Prohibited Transactions. Both ERISA Section 406(a) (party in interest) and 406(b) (fiduciary self-dealing) prohibited transaction claims survived. As to the plaintiff's Section 406(a) claim, the court found the allegations sufficient, holding that the "reasonable compensation" exception in Section 408(b) (as well as PTE 77-3), were affirmative defenses, the burden of proof for which lies with the defendants. Notably, the court also easily accepted that allegations that defendants dealt with plan assets to increase assets under management in order to attract outside investors stated a claim for violation of Section 406(b).

Other Claims. Monitoring and co-fiduciary claims survived, as did prudence/loyalty and prohibited transaction claims for excessive recordkeeping fees. As to the latter, *Krueger* rejected the defendants' attempt to distinguish *Tussey* and held that plaintiffs were entitled to discovery, just as was had in *Tussey*. The plaintiffs' fiduciary breach and prohibited transaction claims based on Ameriprise's sale of its recordkeeping business to Wachovia and subsequent retention of Wachovia as a recordkeeper also survived.[43] Unjust enrichment was the only claim that failed—unrecognized by the Eighth Circuit and seemingly unnecessary because the plaintiffs could and did seek relief under ERISA Section 502(a)(2) and (a)(3), which together provide for recovery of losses to the plan and "appropriate equitable relief"—the remedial scheme intended by Congress in cases like this. In asserting the unjust enrichment claim, the plaintiffs relied on authorities holding that, in the Eighth Circuit, a federal common law action for restitution was available to employers seeking recovery of mistaken payments. The *Krueger* court rejected that logic, however, because the plaintiffs' ERISA claims provided for the relief they sought.

Lessons from Krueger

On the whole, *Krueger* is a pro-plaintiff opinion that rests on solid ERISA principles—including the approach that courts must use in evaluating process-based claims on the pleadings, incorporating the fundamentals of loyalty and prudence. Yet the opinion provides an example of expansion on the factual scenarios that make successful ERISA fee claims. First, hundreds or thousands of investment options cannot insulate a plan's fiduciaries from liability. This holding limits the reach of the Seventh Circuit's decision in *Hecker I*,[44] which affirmed the dismissal of claims against a plan with hundreds of investment options. Second, self-dealing does not just mean taking kickbacks. Using a plan to expand market exposure to proprietary investment options also runs afoul of ERISA.

As the parties move through discovery, the factual support for the plaintiffs' allegations will develop and shed further light on the challenged practices.

Class Certification: *Healthcare Strategies, Inc. v. ING Life Insurance & Annuity Co.* Tackles Class of Plans Issues and Reinforces the Breadth of Fiduciary Status

In *Healthcare Strategies Inc. v. ING Life Ins. & Annuity Co.*, No. 11-282 (D. Conn.) (*HSI II*),[45] Judge Janet C. Hall certified a class of plans in a case involving bundled service provider ING Life Insurance and Annuity Company (ILIAC), whose separate account investment platform was used by thousands of retirement plans. The plaintiff—a plan administrator and fiduciary of the plans—brought class claims alleging fiduciary breaches and prohibited transactions arising out of ILIAC's control over plan assets and extraction of revenue sharing payments from the mutual funds within the

[37] *Hecker v. Deere & Co.*, 556 F.3d 575, 45 EBC 2761 (7th Cir. 2009) (*Hecker I*).

[38] *Renfro v. Unisys Corp.*, 671 F.3d 314, 51 EBC 1609 (3d Cir. 2011).

[39] *Hecker v. Deere & Co.*, 569 F.3d 708, 711, 47 EBC 1097 (7th Cir. 2009) (*Hecker II*).

[40] *Pfeil v. State Street Bank & Trust Co.*, 671 F.3d 585, 591, 52 EBC 1641 (6th Cir. 2012) ("Much as one bad apple spoils the bunch, the fiduciary's designation of a single imprudent investment offered as part of an otherwise prudent menu of investment choices amounts to a breach of fiduciary duty.").

[41] *DiFelice v. U.S. Airways*, 497 F.3d 410, 423, 41 EBC 1321 (4th Cir. 2007) ("[A] fiduciary cannot free himself from his duty to act as a prudent man simply by arguing that other funds . . . could theoretically, in combination, create a prudent portfolio.").

[42] *Krueger*, No. 11-02781, 2012 BL 313619.

[43] *Id.* ("While the corporate business decision to sell ATC to Wachovia is not subject to ERISA regulation, Defendants are not entitled to keep profits that may have resulted from the unlawful use of Plan assets to prop up ATC for its ultimate sale to Wachovia.").

[44] *Hecker v. Deere & Co.*, 556 F.3d 575, 45 EBC 2761 (7th Cir. 2009).

[45] *Healthcare Strategies, Inc. v. ING Life Ins. & Annuity Co.*, No. 11-282, slip. op. (ECF No. 126) (D. Conn. Sept. 26, 2012) (*HSI II*).

separate account investment options that ILIAC offered to 401(k) plans.

Background / Motion to Dismiss (HSI I)

ILIAC's motion to dismiss was denied in large part in 2012.[46] The court declined to dismiss on statute of limitations grounds, but held that fixed and guaranteed accumulation accounts did not hold plan assets and therefore were not subject to ERISA, leaving only separate account claims in the case. The court upheld the jury demand, relying on *Coan v. Kaufman*,[47] for plaintiffs' first count alleging prudence and loyalty breaches based on ILIAC's use of its control over plan assets to generate revenue sharing and other benefits to itself. However, as to the plaintiffs' second count (ERISA Section 406(b) prohibited transaction claims seeking disgorgement of ill-gotten revenue sharing and other compensation) and third count (under ERISA Section 502(a)(3) for non-fiduciary participation in a breach), the court struck the jury demand.

Commonality in HSI II

On class certification, the *HSI II* court easily found numerosity for a class of thousands of plans, moving on to a lengthy commonality analysis.

Fiduciary Status. The court rejected ILIAC's challenges to its fiduciary status, holding that ILIAC controls "which investments are available to the plans and participants and it provides advice about those options."[48] The court found that ILIAC also "controls the investment of separate account assets, determines charges and fees, retains authority to change funds available through the separate account, and to discontinue any fund offered through the separate account."[49] The *HSI* court rejected ILIAC's reliance on *Hecker I*[50] and *Zang v. Paychex*[51] for the proposition that "simple creation of a menu of investment options renders a service provider a fiduciary."[52] Instead, the court cited *Haddock v. Nationwide Fin. Servs., Inc.*,[53] emphasizing its holding that "the defendant's contractual right to modify the menu, rather than any other feature of the contract, determines its status as a fiduciary."[54] As for the "notice" requirement in *HSI*, the court turned to the Department of Labor's Aetna letter,[55] emphasizing the importance of the ability to reject a substitution and terminate services *without a penalty*. In an ironic observation, the court pointed out that "ILIAC's argument that the ability of plans to terminate contracts without a fee varied widely and was a result of individual negotiation of service contracts. . .undercuts its argument that it did not exercise discretion or control in conjunction with its ownership of separate accounts."[56] ILIAC's "individual issues" attack on class certification thus cinched its fiduciary status. The court held that "ILIAC's contractual right to delete and substitute mutual funds from its menu gave it discretion with respect to the administration of the plan sufficient to make it a fiduciary with respect to the allegedly inappropriate receipt of revenue in exchange for the inclusion of those funds on its menu" and that "ILIAC's other arguments are more properly addressed on their merits at a later stage in this litigation."[57]

Plan Assets. The court distinguished *Hecker I*'s holding that revenue sharing payments were not plan assets where they were made from mutual funds to service providers "that were neither the final arbiters of the funds' inclusion in the plans' menu nor the owners of the plan assets,"[58] holding instead that it is a question common to the class "whether ILIAC used the plans' assets held in the separate accounts in its own interest or for its own account."[59] The court also emphasized the well-settled point that reasonableness of compensation is irrelevant to an ERISA Section 406(b) claim.

Causation. In response to ILIAC's argument that it was the plan fiduciaries that actually chose to include funds that made revenue sharing payments, the court held that "Section 406(b) conspicuously lacks a causation requirement."[60]

Defenses and Counterclaims. The court rejected ILIAC's argument that individual defenses, such as the statute of limitations, defeat commonality. Similarly, ILIAC's argument that its counterclaims for contribution, indemnity, and fiduciary breach defeat commonality was rejected, because they "would affect the apportionment of damages among co-fiduciaries, and not the fact of ILIAC's liability."[61]

Typicality and Adequacy

Typicality rested on ILIAC's acceptance of revenue sharing payments from mutual funds in ILIAC's separate accounts. As for adequacy, ILIAC argued that the plan fiduciary plaintiff's interests were antagonistic to the participants' interests. The court disagreed. The court said that ILIAC's argument that if it is guilty of prohibited transactions, the plans would be forced to pay ILIAC's fees in some way that is not illegal under ERISA "deserves no comment."[62] The court also rejected ILIAC's challenge to HSI's ability to pursue

[46] *Healthcare Strategies, Inc. v. ING Life Insurance & Annuity Co.*, No. 11-282, 2012 BL 12023 (D. Conn. Jan. 19, 2012) (*HSI I*).
[47] *Coan v. Kaufman*, 333 F. Supp. 2d 14, 34 EBC 1104 (D. Conn. 2004).
[48] *HSI II*, slip op. at 2.
[49] *Id.* at 3.
[50] *Hecker v. Deere & Co.*, 556 F.3d 575, 45 EBC 2761 (7th Cir. 2009).
[51] *Zang v. Paychex*, 728 F. Supp. 2d 26, 49 EBC 1897 (W.D.N.Y. 2010).
[52] *HSI II*, slip op. at 8.
[53] *Haddock v. Nationwide Fin. Servs., Inc.*, 262 F.R.D. 97 (D. Conn. 2009), *vacated on other grounds by Nationwide Life Ins. Co. v. Haddock*, 460 Fed. App'x 26 (2d Cir. 2012).
[54] *HSI II*, slip. op. at 9.
[55] DOL Op. 97-16A (May 22, 1997).
[56] *HSI II*, slip op. at 10.
[57] *Id.* at 11.
[58] *Id.* at 11 n. 5.
[59] *Id.* at 12-13.
[60] *Id.* at 13-14.
[61] *Id.* at 15.
[62] *Id.* at 17.

injunctive relief given that it had terminated its contract with ILIAC, but suggested HSI find a co-plaintiff "with unquestioned capacity to seek injunctive relief" within 60 days.[63]

Rule 23(b)

HSI sought class certification under Rule 23(b)(1) or 23(b)(3). Building on its jury trial ruling on the pleadings, the court found that because of the availability of "damages at law" for plaintiffs' ERISA Section 502(a)(2) breach claims, Rule 23(b)(3) would be the more appropriate provision for certification. The court found the predominance prong satisfied because whether or not revenue sharing payments are prohibited transactions is a legal and factual common question, and ILIAC "offers only a few versions of ILIAC's MAP contracts that are at issue in this case."[64] Thus, absolute uniformity of contracts is not required across a class of plans. ILIAC challenged superiority by arguing that ERISA's fee shifting provision " 'eviscerates' HSI's 'cost of litigating' argument," but the court disagreed.[65]

Sufficiency of Contribution and Indemnity Counterclaims

HSI II also addressed ILIAC's five counterclaims: for contribution and indemnity under ERISA, as well as for common law contribution and indemnity, and for breach of fiduciary duty under ERISA—all of which depend on a finding of liability against ILIAC and that HSI as a co-fiduciary can also be held liable for ILIAC's conduct. Siding with *Haddock v. Nationwide Fin. Servs., Inc.*[66] and following *Chemung Canal Trust Co. v. Sovran Bank/Maryland*,[67] the court held that fiduciary contribution and indemnity claims are permitted under ERISA. The court also found that ILIAC would be allowed to seek indemnity from HSI up to the amount of benefit to ILIAC for count one, but that ILIAC's counterclaims did not satisfy *Iqbal*[68] because ILIAC must plausibly plead that "HSI was not so substantially less at fault than ILIAC that HSI would be entitled to indemnity from ILIAC under the Restatements."[69] Finally, the court found that ILIAC's counterclaim for fiduciary breach against HSI failed to satisfy *Iqbal* because any losses to the plan would be because of its own breaches. ILIAC was granted leave to replead.

Lessons from HSI II

Overall, *HSI II* is a win for plaintiffs and provides a solid foundation for certifying class of plans cases arising out of fees charged to the significant share of the 401(k) market that uses bundled platforms built on insurance companies' separate accounts. Separate accounts are clearly subject to ERISA's fiduciary standards and funds within them are plan assets as a matter of law.[70] Accordingly, the fees charged in these structures are ripe for scrutiny, and prohibited transactions by *fiduciaries* who manage separate accounts are not subject to a reasonableness exception. The level of authority a fiduciary service provider has to change or remove investment options remains a critical factor in determining fiduciary status. Control over plan assets by way of the power to select, swap out, and delete funds, as well as the ability to penalize rejection of the service provider's choice or self-deal to unilaterally affect compensation, remain key questions in establishing fiduciary status—and prohibited transactions—in this context.

Other Developments

ILIAC filed a motion for summary judgment, as well as a motion for certificate of appealability on the jury trial issue. The court denied the latter. The court allowed intervention by the DeRosa Corporation as an additional named plaintiff, and the plaintiffs filed an amended complaint in December of 2012. The court transferred the case to Boston on Jan. 10, 2013. Discovery was reopened to accommodate DeRosa's addition to the case. ILIAC answered the amended complaint on Jan. 10, 2013, and the plaintiffs moved to dismiss ILIAC's counterclaims on January 24. Briefing on that issue was completed on Feb. 26, 2013. The parties are briefing summary judgment and have suggested a trial date on or after Sept. 1, 2013.

Class Certification and Summary Judgment: *Glass Dimensions v. State Street* Focuses on the Defendants' Conduct in Securities Lending

Glass Dimensions, No. 10-10588 (D. Mass.), is a class of plans case brought by a fiduciary challenging the compensation collected by State Street in connection with collective trust investment options involved in securities lending.[71] Plaintiff alleged that State Street's retention of 50 percent of the "spread" earned on securities lending transactions was excessive, far exceeded industry standards, and that the defendants were overcompensated.[72] Plaintiff alleged as well that defendants "negotiated with themselves the terms of their compensation,

[63] *Id.* at 18-20.
[64] *Id.* at 24.
[65] *Id.* at 25.
[66] *Haddock v. Nationwide Fin. Servs., Inc.*, 570 F. Supp. 2d 355, 44 EBC 1926 (D. Conn. 2008).
[67] *Chemung Canal Trust Co. v. Sovran Bank/Maryland*, 939 F.2d 12, 14 EBC 1169 (2d Cir. 1991).
[68] *Ashcroft v. Iqbal*, 556 U.S. 662 (2009).
[69] *HSI II*, slip op. at 42; *see also id.* at 29-39.
[70] *See* ERISA Section 401(c)(5), 29 U.S.C. § 1101(c)(5); 29 C.F.R § 2550.401c-1(d)(2)(c) (definition of "plan assets" for insurance companies); 29 C.F.R. § 2550.401c-1(g) (prudence standard applies); 29 C.F.R. § 2510.3-101(h)(iii) (assets in insurer's separate account are plan assets).
[71] Though like mutual funds in that they pool together the investments of many institutional investors, collective investment trusts are distinguishable from mutual funds in that the managers of collective investment trusts are held to ERISA fiduciary standards. Thus, as with separate accounts, the investment by ERISA plans in collective trust investment vehicles confers fiduciary status with respect to the investing plans on those who run the collective trusts. *See* 29 C.F.R. § 2510.3-101(a)(2); 29 C.F.R. § 2510.3-101(h)(1)(ii).
[72] *Glass Dimensions, Inc. v. State Street Bank & Trust Co.*, 285 F.R.D. 169, 2012 BL 342717 (D. Mass. 2012) (*Glass Dimensions I*).

discretion, authority, and . . . liability," resulting in them setting their own unreasonable compensation.[73]

In August of 2012, the court in *Glass Dimensions* resolved both the defendants' motion for summary judgment with respect to standing and the plaintiff's motion for class certification in the plaintiff's favor.

Summary Judgment

State Street argued that plaintiff only had standing to sue on behalf of the three lending funds in which it invested directly, but that plaintiff lacked standing to sue on behalf of the 257 funds in which it did not directly invest. The court's August 2012 order rejected the defendants' arguments because the defendants' common conduct and the plaintiff's clear relationship with each defendant differentiated this case from cases upon which the defendants had relied. Under First Circuit law, the plaintiff only had to establish constitutional standing with respect to each defendant. Once constitutional standing is established, the question of proceeding is one for Rule 23.

Class Certification

The court certified a class of plans. In its commonality discussion, the *Glass Dimensions* court rejected the defendants' arguments that the reasonableness of their compensation could not be subject to common proof and that compensation had to be evaluated on "an individual basis for each fund."[74] The court held that the fee was imposed "en masse without regard to the individual characteristics of each ERISA plan investor, or of the funds themselves."[75] Additionally, whether the defendants were fiduciaries under ERISA was stated as a common question that the court has not yet answered. As to typicality, the court found that it made no difference whether defendants negotiated their fee with some plans and "simply implemented it for others," because that does not affect the plaintiff's incentives in pursuing the litigation. Like *HSI II*, the *Glass Dimensions* court certified the class under Rule 23(b)(3), finding that the common issue of the fee's reasonableness predominated.

Other Developments and Summary Judgment Part Deux

On Jan. 14, 2013, the court issued an order denying the Goodyear Trustees' motion to intervene as plaintiffs, in part because the Goodyear Plan was not a member of the certified class.[76] In the same order, the court ruled on defendants' motion to strike expert reports, finding no harm in a late affirmative report and finding a separate report a proper rebuttal. Finally, the court declined to strike the defendants' Prohibited Transaction Exemption 2006-16 affirmative defense for failure to provide discovery and instead ordered discovery and time to supplement expert reports.

On March 21, 2013 (ECF No. 228), the court denied all pending motions for summary judgment after a hearing. On State Street's summary judgment motion, the court held that the plaintiff's claims were not barred by ERISA's three-year statute of limitations, that plaintiff offered sufficient evidence that State Street was a fiduciary with respect to its own compensation, that State Street was not entitled to summary judgment on plaintiff's fiduciary breach claim, that there were material issues of fact as to whether Prohibited Transaction Exemption 2006-16 was complied with, and that disputes about the measure of damages precluded summary judgment. Plaintiff had moved for summary judgment on prohibited transaction issues mirroring State Street's, but here too, the court found that there were material issues of fact regarding State Street's compliance with PTE 2006-16. Plaintiff also submitted as supplemental authority on the issue of fiduciary status (ECF No. 230) the motion to dismiss opinion in *Santomenno v. Transamerica Life Ins. Co.*, No. 12-2782 (C.D. Cal.).[77]

Summary Judgment: *Borroughs v. Blue Cross* Highlights Undisclosed Fees in a Welfare Plan

Borroughs Corp. v. Blue Cross Shield of Mich., Nos. 11-12565 & 11-12557 (E.D. Mich.),[78] arises out of Blue Cross's contracts for claims administration services and network access for self-funded employee health benefit plans. Though not a defined contribution plan case, it involves a fiduciary using its power to hide and collect a hidden fee that did not show up on customer statements, suggesting potential fertile ground for claims against 401(k) plan fiduciaries who similarly fail to disclose their fees.

Plaintiffs—the plan sponsor and the plan—alleged that from 1994 to the present, "Blue Cross employed a 'bevy of artifices' to hide" certain fees that Blue Cross paid itself as additional administrative compensation.[79] The parties cross-moved for summary judgment, and Judge Victoria A. Roberts granted summary judgment to the plaintiffs on their ERISA prohibited transaction claim—setting the stage for future analysis of hidden fees under ERISA—while finding their state law claims preempted and finding remaining issues of fact as to the statute of limitations defense.

Fiduciary Status

The court began by finding Blue Cross was a fiduciary when it allocated fees from plan assets to itself, relying in part on the factually related *Pipefitters Local 636 Ins. Fund v. Blue Cross Blue Shield of Mich.*[80] The

[73] *Id.* at 173.
[74] *Id.* at 177.
[75] *Id.*
[76] *Glass Dimensions, Inc. v. State Street Bank & Trust Co.*, No. 10-10588-JLT, 2013 BL 9897 (D. Mass. Jan. 14, 2013) (*Glass Dimensions II*).

[77] *See infra.*
[78] The associated case is *Hi-Lex Controls Inc. v. Blue Cross and Blue Shield of Mich.*
[79] *Borroughs Corp. v. Blue Cross Shield of Mich.*, Nos. 11-12565 & 11-12557, 53 EBC 2829 (E.D. Mich. Sept. 7, 2012) (*Borroughs I*).
[80] *Pipefitters Local 636 Ins. Fund v. Blue Cross Blue Shield of Mich.*, 654 F.3d 618, 52 EBC 1590 (6th Cir. 2011), *cert. denied*, 132

Borroughs court found Blue Cross's control over the ERISA plan's money dispositive: "The fact that Blue Cross was able to allocate to itself an administrative fee demonstrates its control over plan assets."[81] Blue Cross argued that *Seaway Food Town, Inc. v. Medical Mutual of Ohio*[82] absolved it of fiduciary status because the contracts granted Blue Cross the "unilateral right to retain the Disputed Fees." The court rejected this argument because "*Seaway* holds that adherence to a contractual term does not give rise to fiduciary status '*unless the term authorizes the party to exercise discretion with respect to that right.*' "[83] Because Blue Cross could determine the amount of the fee, it had the necessary authority over plan assets to be a fiduciary. The court rejected Blue Cross's attempt to distinguish the discretion whether or not to charge a fee from the discretion to determine the amount of an authorized fee, relying on *Charters v. John Hancock Life Ins. Co.*[84] *Borroughs* also rejected Blue Cross's reliance on *McLemore v. Regions Bank*[85] as limited to banks.[86]

Prohibited Transactions.

The *Borroughs* court relied on *Patelco Credit Union v. Sahni*[87] in finding that Blue Cross's determination of its own administrative fee, which it collected from plan assets, established an ERISA Section 406(b) prohibited transaction. The court emphasized the "absolute bar against self dealing" enshrined by ERISA Section 406(b).[88] The court held that "[w]hether Blue Cross calculated its fee according to a set methodology or pulled numbers out of the sky, it still unilaterally dealt with plan assets for its own benefit. . . .This sort of self-dealing is a *per se* breach of Section 1106(b)(1)."[89]

Impact of Borroughs

Looking to the opinion in *Borroughs I* and the well-settled principles on which it relies regarding control over fees, service providers who set their own fees can count on fiduciary status. And whether they merely unilaterally set their fees, or also hide them, they will easily be liable for Section 406(b) prohibited transactions—in the context of 401(k) plans as well as welfare plans. Such claims will be especially significant as previously undisclosed fees come to light in the context of Section 408(b)(2) disclosures.

Counterclaims Futile

On Jan. 22, 2013, the court denied the defendants' motion to assert counterclaims in *Borroughs* and the associated *Hi-Lex* case to seek contribution and indemnification from the plaintiffs.[90] The court held that contribution and indemnification are not allowed under ERISA, coming down on the opposite side of the circuit divide as the court in *HSI II*.

Other Developments

In early 2013, plaintiffs won discovery of claims data and filed a fourth motion to compel. Trials in the associated cases are scheduled for 2013.

Appellate Decisions

Several appeals were resolved in ERISA fee cases in 2012, touching on a number of issues that will bear on ongoing and future litigation, particularly as service provider disclosures emerge under the rules. Questions of fiduciary status will persist, but nonfiduciaries, even those who are not "parties in interest," will face ERISA liability under Section 502(a)(3) for participation in the ERISA violations of fiduciaries. In the certification landscape for classes of plans, 23(b)(2) is out and 23(b)(3) is in. And defendants' attempts to put up roadblocks to participant claims pursuant to ERISA Sections 502(a)(2) and (a)(3) by insisting on presuit demands and joinder of trustees should be a thing of the past.

Section 406(b)(3) Prohibited Transactions and Liability for Nonfiduciaries who are not "Parties in Interest": Nat'l Sec. Sys., Inc. v. Iola

In *Nat'l Sec. Sys., Inc. v. Iola*,[91] the Third Circuit addressed the scope of who can be subject to "appropriate equitable relief" under ERISA Section 502(a)(3), finding that nonfidcuiaries who are also not "parties in interest" may be on the hook for participating in kickbacks that violate ERISA Section 406(b)(3).

The facts involve a tax avoidance scheme. One of the defendants, financial planner James Barrett, induced the plaintiffs to adopt an employee welfare benefit plan known as "EPIC." EPIC's tax benefits were illusory, and while the scheme looked like a welfare plan, it was a method of deferred compensation. Defendant Tri-Core received commissions from the life insurance policies that were investment vehicles for the plan. Barrett marketed the EPIC plan to plaintiffs. The claims centered on allegations that Tri-Core and Barrett misrepresented tax risks and benefits, concealed their commissions from plaintiffs' contributions to the plan, and misrepresented the ability of plan participants to access conversion credits.

S. Ct. 1757 (2012). In *Pipefitters*, the Sixth Circuit reversed a class of plans certification under Rule 23(b)(3), finding that individualized findings regarding fiduciary status defeat class certification, as well as under 23(b)(1)(A), finding no risk of inconsistent standards of conduct.

[81] *Borroughs I*, Nos. 11-12565 & 11-12557, 53 EBC 2829.

[82] *Seaway Food Town, Inc. v. Medical Mutual of Ohio*, 347 F.3d 610, 31 EBC 1609 (6th Cir. 2003).

[83] *Borroughs I* (emphasis in original).

[84] *Charters v. John Hancock Life Ins. Co.*, 583 F. Supp. 2d 189, 197, 45 EBC 1183 (D. Mass. 2008) (control over factors affecting compensation are enough).

[85] *McLemore v. Regions Bank*, 682 F.2d 414, 53 EBC 2313 (6th Cir. 2012) (bank that collected contractually owed fees not a fiduciary).

[86] *Borroughs I.*

[87] *Patelco Credit Union v. Sahni*, 262 F.3d 897, 26 EBC 2060 (9th Cir. 2001).

[88] *Borroughs I.*

[89] *Id.*

[90] *Hi-Lex Controls Inc. v. Blue Cross and Blue Shield of Mich.*, Nos. 11-12557, 11-12565, 53 EBC 2829 (E.D. Mich. Jan. 22, 2013) (*Borroughs II*).

[91] *Nat'l Sec. Sys., Inc. v. Iola*, 700 F.3d 65, 2012 BL 294218 (3d Cir. 2012).

In a lengthy *Harris Trust*[92] analysis of the scope of ERISA Section 502(a)(3), the *Iola* court went through the development of the law and various courts' consideration of whether *Harris Trust* doctrine applies only to violations of ERISA Section 406(a) or goes beyond, all of them concluding that it does.[93] Applying that history to the claim against Barrett for participation in a Section 406(b)(3) prohibited transaction, the court distinguished (and discounted) its prior ruling in *Renfro*[94] as irrelevant to prohibited transaction claims (but, oddly, suggested *Renfro* is still capable of limiting liability for nonfiduciary participation in Section 404(a) breaches). The court confirmed that *Harris Trust* is grounded in Section 502(a)(3), not Section 406(a), and therefore does not require a liable party to be a "party in interest."[95]

The *Iola* court also went through an exhaustive analysis of Barrett's ERISA Section 408(c)(2) "reasonable compensation" argument, and concluded, deferring to the Department of Labor, that it was "not an independent reasonable compensation exemption" and did not shield him from Section 406(b)(3) liability, because Section 406(b) was "unyielding."[96]

The court's Section 502(a)(3) remedies analysis was interesting. In discussing whether disgorgement of only half of collected commissions (instead of all commissions) was appropriate, the court held that disgorgement of ill-gotten profits/commissions was an appropriate equitable remedy. Taking this concept at face value, the court's constructive trust analysis belied frequently asserted defenses that any commission-like funds sought from a non-fiduciary are merely fungible cash, not traceable, and unable to be identified and, therefore, cannot be disgorged. The *Iola* court didn't seem to think that was a problem.

A motion to stay the mandate was granted while the defendants see if the Supreme Court will accept review, and their petition for a writ of certiorari was filed on Feb. 5, 2013 (S. Ct. Case number 12-975). There likely will be more to come in 2013.

Class Certification Remand: Nationwide v. Haddock

In the long-running *Haddock* litigation, the district court certified a class of 24,000 plans on Nov. 6, 2009, finding that certification of an opt-out 23(b)(2) class was appropriate, given the equitable monetary disgorgement and injunctive relief sought by the plaintiffs.[97] In so doing, the district court rejected Nationwide's argument that it did not act on grounds that apply generally to the class and that a class-by-class inquiry is necessary to determine its fiduciary status.

During the pendency of the defendants' appeal, *Wal-Mart Stores, Inc. v. Dukes*[98] came out restricting the reach of Rule 23(b)(2). In light of *Wal-Mart*, the Second Circuit vacated the district court's order and remanded the class certification question:

> In the case at bar, if plaintiffs are ultimately successful in establishing Nationwide's liability on the disgorgement issue, the district court would then need to determine the separate monetary recoveries to which individual plaintiffs are entitled from the funds disgorged. This process would require the type of non-incidental, individualized proceedings for monetary awards that *Wal–Mart* rejected under Rule 23(b)(2).[99]

The district court now must determine whether a 23(b)(3) class is appropriate.

The opinion in *HSI II*—hailing from the same district as *Haddock*—is likely to provide a roadmap to the court in reconsidering class certification for a class of plans. It will be interesting to watch how the *Haddock* court treats the monetary portion of relief. Will *Haddock* stick to the equitable disgorgement framework when discussing monetary relief for ill-gotten fees or will the court adopt the "legal damages" construction used by the *HSI II* court to shore up the appropriateness of Rule 23(b)(3)?

Pre-suit Demands and Joinder of Trustees Not Required: Santomenno v. John Hancock Life Ins. Co.

In *Santomenno v. John Hancock Life Ins. Co.*, the district court dismissed the participant plaintiffs' ERISA claims for excessive fees charged on group annuity contract investments in their 401(k) plan on the basis that they had not made a pre-suit demand.[100] The Third Circuit reversed and the Supreme Court denied review.[101]

The Third Circuit's holding was grounded in the text of ERISA—which is silent as to pre-suit demands and mandatory joinder of trustees. The Third Circuit noted that no Court of Appeals has found pre-suit demand a requirement for civil actions brought under ERISA Section 502(a)(2) or (a)(3).[102]

The *Santomenno* court also relied on the purpose of ERISA: "One reason for this lack of a demand requirement for Section 502(a)(2) and (a)(3) claims is that the protective purposes of ERISA would be subverted if the section covering fiduciary breach required beneficiaries to ask trustees to sue themselves."[103] The court noted that "[i]n addition to the text, structure, and purpose of ERISA, the legislative history of the statute also indi-

[92] *Harris Trust & Sav. Bank v. Salomon Smith Barney Inc.*, 530 U.S. 238, 24 EBC 1654 (2000).
[93] *Iola*, 700 F.3d at 86-90.
[94] *Renfro v. Unisys Corp.*, 671 F.3d 314, 51 EBC 1609 (3d Cir. 2011).
[95] *See Iola*, 700 F.3d at 93-96.
[96] *Id.*
[97] *Haddock v. Nationwide*, 262 F.R.D. 97, 48 EBC 1194 (D. Conn. 2009).
[98] *Wal-Mart Stores, Inc. v. Dukes*, 131 S. Ct. 2541, 180 L. Ed. 2d 374 (2011).
[99] *Nationwide Life Ins. Co. v. Haddock*, 460 F. App'x 26, 29 (2d Cir. 2012).
[100] *Santomenno v. John Hancock Life Ins. Co.*, No. 10-1655, 51 EBC 2123 (D.N.J. May 23, 2011).
[101] *Santomenno v. John Hancock Life Ins. Co.*, 677 F.3d 178, 52 EBC 2807 (3d Cir. 2012), *cert. denied*, 133 S. Ct. 529 (2012).
[102] *Id.* at 188 (citing *Katsaros v. Cody*, 744 F.2d 270, 5 EBC 1777 (2d Cir. 1984); *Licensed Div. Dist. No. 1 MEBA/NMU v. Defries*, 943 F.2d 474, 14 EBC 1736 (4th Cir. 1991)).
[103] *Santomenno*, 677 F.3d at 189.

cates that Congress did not intend to impose obstacles such as pre-suit demand or mandatory joinder of trustees with respect to claims brought under Section 502(a)."[104] The Department of Labor's amicus brief appears to have been persuasive to the court on all of these points.

On remand, this class of plans case was reopened for proceedings in the district court in June 2012. Defendants' motion to dismiss the plaintiffs' second amended complaint was filed on Dec. 14, 2012. Briefing was completed in February 2013.

Settlements

Braden v. Wal-Mart

The district court entered an order of final approval of the settlement of the four-year *Braden v. Wal-Mart* excessive fee litigation on March 19, 2012.[105] The settlement included a cash payment of $13.5 million from the Wal-Mart and Merrill Lynch defendants, the net proceeds of which will be used to offset future plan expenses that otherwise would be charged to participant accounts. In addition, and building on significant changes that Wal-Mart already had made to the plan investment lineup since 2008, the settlement provided for the following injunctive relief:[106]

- Continued retention of a consultant or independent adviser who is not otherwise affiliated with Wal-Mart and who has acknowledged in writing fiduciary status with the plan within the meaning of ERISA Section 3(21)(A), to provide independent advice and recommendations on selection and monitoring of Plan Investment Options, as well as annual review of the consultant or independent adviser for conflicts of interest;
- Continued availability on the Wal-Mart and Merrill Lynch websites of web-based investment education resources, including a retirement planning calculator, to participants of the plan;
- Continued removal from the Plan's Investment Options, as well as a prohibition on adding as Investment Options, funds that are retail mutual funds, funds that pay 12b-1 fees, and funds that provide revenue sharing, per-position or per-participant sub-transfer agent fees, or other fees, to any party in interest as defined in ERISA Section 3(14), including the plan's trustee or recordkeeper;
- As of the settlement date, the plan offers two index funds on its core menu. The Retirement Plans Committee will consider, where and when appropriate, adding other low-cost, passively managed investment vehicles to the Plan Investment Options;
- Compliance with the Section 404(a) disclosure regulations, which shall include posting information about the Plan's Investment Options in the format set forth in the rule's Model Comparative Chart, on www.benefits.ml.com. An active link to the Department of Labor's "A Look At 401(k) Plan Fees" publication will also be included in the Comparative Chart or in proximity to the online version of the Comparative Chart on www.benefits.ml.com; and
- The Retirement Plans Committee shall post a link on www.benefits.ml.com to the SEC Cost Calculator found at http://www.sec.gov/investor/tools/mfcc/get-started.htm, with such link located in proximity to the online version of the Comparative Chart and with guidance to participants on how to complete the SEC Cost Calculator for the Plan Investment Options.

The district court approved an attorneys' fee award of 30 percent, awarded costs, and awarded the sole named plaintiff $20,000 as requested. The district court also considered and rejected the arguments by an objector who opposed the settlement's plan of allocation, and thereafter denied his motion for attorneys' fees.[107]

George v. Kraft

George v. Kraft began in 2006 and involved allegations by plan participants that recordkeeping and administrative fees associated with their retirement plan were unreasonable and excessive and that the plan improperly included actively managed funds. On the heels of the Seventh Circuit opinion,[108] which reversed in part summary judgment that had been granted to the defendants, the parties settled *George, et al v. Kraft Foods Global, Inc., et al.*, Nos. 07-CV-01713 (*George I*) and the closely related No. 08-CV-03799 (*George II*). The Seventh Circuit had remanded the case after finding that because a fiduciary's failure to exercise discretion is actionable under ERISA, plaintiffs' claims related to "transactional drag" required analysis regarding whether fiduciaries made a decision, as well as whether a prudent fiduciary would have made a decision at the time.[109] The court also reversed and remanded the issue of the reasonableness of Hewitt's recordkeeping fees and whether periodic competitive bids were required to satisfy the duty of prudence. Regarding float, however, the court affirmed summary judgment for defendants, finding that the defendants requested and received dollar amount reports regarding the amount of float collected by State Street, thus highlighting a key factual difference when compared to *Tussey*, where the amount was never ascertained and could not have been deemed reasonable.

[104] *Id.*

[105] *Braden v. Wal-Mart Stores Inc.*, No. 08-3109, Final Order and Judgment (W.D. Mo. Mar. 19, 2012) (ECF No. 258).

[106] *See Braden v. Wal-Mart Stores, Inc.*, No. 08-3109, Settlement Agreement, docketed as Exhibit A to Motion for Order Preliminarily Approving Class Action Settlement and Setting Hearing for Final Approval. No. 08-3109 (W.D. Mo. Dec. 2, 2011) (ECF No. 229-1).

[107] *Braden v. Wal-Mart Stores Inc.,* No. 08-3109, Final Order and Judgment (W.D. Mo. Mar. 19, 2012) (ECF No. 258); *Braden v. Wal-Mart Stores Inc.,* No. 08-3109, Order (W.D. Mo. April 13, 2012) (ECF No. 261).

[108] *George v. Kraft Foods Global Inc.*, 641 F.3d 786, 50 EBC 2761 (7th Cir. 2011).

[109] *Id.* at 796-97.

The settlement, for which final approval was granted on June 26, 2012, provides for a $9.5 million settlement fund, as well as the following injunctive relief:[110]

- Defendants will continue to not offer "retail" mutual funds as core investment options in the Plan;
- Defendants will make enhanced fee disclosures as required by the Department of Labor;
- Defendants will continue to limit the cash investments of the company stock funds;
- Defendants will remove the mutual fund known as the "Balanced Fund" from the plan and not reintroduce that mutual fund to the plan; and
- Defendants will implement the results of a recent competitive bidding process by replacing the existing recordkeeper with a less expensive recordkeeper, thus reducing administrative fees paid by plan participants.

The court approved awards of $15,000 to each of the four named plaintiffs and awarded attorneys' fees of one-third of the settlement, as well as costs.[111]

Early Developments and What Else to Watch in 2013

Cases with Significant Activity in 2013

In the quickly developing field of ERISA fee litigation, it is unsurprising that a large number of cases and important issues remain unresolved. The following are some cases to watch in 2013. Some saw significant activity in the early months of 2013, and many may develop further as 2013 progresses.

David v. Alphin, No. 11-2181 (4th Cir.)

The year 2013 started with the decision in *David v. Alphin*.[112] On Jan. 14, 2013, the Fourth Circuit affirmed summary judgment on the plaintiffs' fiduciary breach and prohibited transaction claims, which had challenged both the initial selection of allegedly imprudent and defendant-affiliated funds and the subsequent failure to remove them.

The opinion accepted defendants' statute of limitations challenge on the "removal" claims, holding that "the alleged prohibited transactions and breach could only be based on the initial selection of the funds."[113] The court thus conflated initial selection with failure to remove, holding that all the claims, as the plaintiffs pleaded the case, related back to the date of initial selection. So the "initial selection claim" was barred by the statute of limitations as well. While a victory for defendants, the opinion's reach is limited. The court specifically held that "we do not decide whether ERISA fiduciaries have an ongoing duty to remove imprudent investment options in the absence of a material change in circumstances."[114]

This *David* opinion raises the question of how best to frame breach and prohibited transaction claims to avoid a similar result. The Department of Labor clearly disagrees with the idea that an initial selection can immunize an imprudent fund once the statute of limitations runs, as calculated from the initial selection date. In its amicus brief, DOL argued that there is a palpable difference between challenging initial inclusion and challenging separate and repeated failures to remove a fund, the latter of which are violations of the ongoing duties of prudence and loyalty.[115] Even if courts ultimately do not accept DOL's view that selection and failure to remove should not be conflated, future plaintiffs can avoid the reach of *David* by alleging facts about the *fiduciary acts* and *transactions* that occurred when fees were collected by plan service providers from imprudent funds long after their initial selection and when decisions were made by investment fiduciaries to keep the funds on the menu.

A petition for rehearing en banc was filed Feb. 28, 2013, and denied on March 12, 2013. A Supreme Court bid could be next.

Tibble v. Edison, Nos. 10-56406, 10-56415 (9th Cir.)

Tibble produced the next big appellate decision of 2013, on the heels of *David*. It involves claims of excessive fees brought by plan participants for violations of the duties of prudence and loyalty arising under ERISA Section 404 and for prohibited transactions in violation of ERISA Section 406. The district court dismissed the Section 406(b)(3) prohibited transaction claims on summary judgment and held that ERISA's six-year statute of limitations barred claims involving funds first made available prior to the period of limitations.

Three issues proceeded to trial in *Tibble* in October 2009: (1) whether defendants violated their duty of prudence by selecting certain retail (rather than institutional) mutual funds with favorable revenue-sharing arrangements but higher fees; (2) whether defendants violated their duties of prudence and loyalty by failing to switch into institutional share classes of certain funds; and (3) whether defendants breached their duty of prudence by investing in a money market fund with allegedly excessive management fees.[116] On July 8, 2010 the district court issued its findings of fact and conclusions of law, holding that defendants breached their fiduciary duties as to the first of these, but not the second or third. The court found no evidence on the

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[110] *George v. Kraft Foods Global, Inc.*, Nos. 08-3799 & 07-1713, Final Order and Judgment (N.D. Ill. June 26, 2012) (ECF No. 349); *see also George v. Kraft Foods Global, Inc.*, Nos. 08-3799 & 07-1713, Settlement Agreement, docketed as an Exhibit (ECF No. 328) to the parties' Joint Motion for Preliminary Approval of Settlement.

[111] *George v. Kraft Foods Global Inc.*, Nos. 08-3799 & 07-1713, Order Regarding Plaintiffs' Application for Attorneys' Fees and Reimbursement of Expenses (N.D. Ill. June 26, 2012) (ECF No. 350).

[112] *David v. Alphin*, 704 F.3d 327, 54 EBC 2437 (4th Cir. 2013).

[113] *Id.* at 340.

[114] *Id.* at 341.

[115] Brief of the Secretary of Labor as Amicus Curiae in Support of Plaintiff-Appellant Urging Reversal at 22-28, *David v. Alphin*, No. 11-2181 (4th Cir. Dec. 28, 2011).

[116] *Tibble v. Edison Int'l*, No. 07-5359, 49 EBC 1725 (C.D. Cal. July 8, 2010) (*Tibble I*).

record of improper consideration of revenue sharing in fund selection. Nevertheless, the court found on the merits that defendants breached their duty by selecting expensive retail funds because participants paid "wholly unnecessary fees." The *Tibble* court also rejected the notion that utilization of an outside consultant absolves a fiduciary of any liability. The court was equally unpersuaded by defendants' claims of mandatory investment minimums, holding that "the only way a fiduciary can obtain a waiver of the investment minimum is to call and ask for one."[117]

The court entered judgment, awarding about $371,000 in damages to the plaintiffs and ordering the defendants to replace a retail share mutual fund with an institutional class share.[118] Plaintiffs have appealed to the extent that this judgment, the post-trial findings of fact and conclusions of law, and pre-trial orders on summary judgment find in favor of defendants.

Both DOL and the AARP filed amicus briefs in support of the plaintiffs-appellants, as did two groups in support of Edison. The case was argued on Nov. 6, 2012, before Judges Alfred T. Goodwin, Diarmuid F. O'Scannlain, and Jack Zouhary. On Jan. 16, 2013, Edison submitted the Fourth Circuit's decision in *David v. Alphin*[119] as supplemental authority on the statute of limitations and prohibited transactions issues.

On March 21, 2013, the Ninth Circuit affirmed the judgment of the district court in a 50-page opinion covering a variety of important issues in ERISA litigation.[120]

Regarding the statute of limitations issue, the panel rejected both parties' arguments. On the issue of when the statute of limitations begins to run, the court held that there can be no "continuing violation theory" in ERISA Section 413,[121] and so the date of initial inclusion of a fund in a plan's lineup is the operative date for "claims asserting imprudence in the design of the plan menu."[122] However, the court made clear that subsequent evidence of "significant changes in conditions" that should have prompted a full review of plan investment options (which necessarily included the option of removal) could establish a subsequent breach.[123] The court's holding, therefore, did "not alter the duty of fiduciaries to exercise prudence *on an ongoing basis*."[124] On Edison's request for application of the three-year statute of limitations, the court held that "actual knowledge" requires " 'some knowledge of how the fiduciary selected the investment.' "[125] Therefore, "mere notification that retail funds were in the Plan menu falls short of providing 'actual knowledge of the breach or violation.' "[126]

The court also rejected Edison's view that ERISA Section 404(c),[127] ERISA's safe harbor defense, eviscerated the plaintiffs' entire case. The Ninth Circuit afforded *Chevron* deference to DOL's 1992 regulation stating that a breach or loss is only insulated by Section 404(c) where it is "the 'direct and necessary result' of the action by the beneficiary."[128] DOL's position articulated in 1992 (and later codified in the Code of Federal Regulations) that limiting or designing investment options is a fiduciary act, and not a direct or necessary result of participant action, carried the day.

In refusing to review the district court's certification of a class, the Ninth Circuit declined to consider application of *Spano*, because Edison did not properly raise that issue below.

Regarding the merits of the plaintiffs' claims, the Ninth Circuit affirmed the district court's summary judgment and bench trial rulings. The court began by holding that a plan administrator who is granted interpretive authority by a plan document is entitled to an abuse of discretion standard of review, a principle arising out of trust law. Under this standard, the use of revenue sharing to offset plan expenses was not unreasonable. Nor were revenue sharing payments a Section 406(b)(3) prohibited transaction, because they were not "consideration." The court went on to hold that it was not an abuse of discretion to include retail mutual funds in the lineup on this record and that the range of fees at issue was not "out of the ordinary enough to make the funds imprudent."[129] However, the court made clear that revenue sharing arrangements and funds charging 12b-1 fees could establish imprudence where those factors made funds more expensive or benefitted fiduciaries. The court affirmed the district court's findings for Edison regarding the short-term investment fund and plaintiffs' challenge to the unitized stock investment. Finally, the court affirmed the finding after trial that it had been imprudent to include retail-class shares of three specific funds because the fiduciaries had "failed to investigate the possibility of institutional-class alternatives."[130] In rejecting Edison's attempt to avoid liability because it used an investment consultant for advice, the Ninth Circuit described the role of that consultant and then held:

> We offer this background to illustrate a point, which, though it should be unmistakable, seems to have eluded Edison in its briefing. HFS is its consultant, not the fiduciary. "As Judge Friendly has explained, independent expert advice is not a 'whitewash.' " *Shay*, 100 F.3d at 1489 (quoting *Donovan v. Bierwirth*, 680 F.2d 263, 272 (2d Cir.1982)). Our *Shay* factors recognize this by not simply requiring that the fiduciary (1) probe the expert's qualifications, and (2) furnish the expert with reliable and complete information, but also

[117] *Id.*

[118] *Id.*; *see also Tibble v. Edison Int'l*, No. 07-5359 (C.D. Cal. Aug. 9, 2010) (ECF Nos. 417, 418) (*Tibble II*).

[119] *David v. Alphin*, 704 F.3d 327, 54 EBC 2437 (4th Cir. 2013).

[120] *Tibble v. Edison*, No. 10-56406, 2013 BL 76391 (9th Cir. Mar. 21, 2013) (*Tibble III*).

[121] 29 U.S.C. § 1113.

[122] *Tibble III.*

[123] *Id.*

[124] *Id.* (emphasis added).

[125] *Id.* (citing *Brown v. Am. Life Holdings, Inc.*, 190 F.3d 856, 859 (8th Cir. 1999).

[126] *Id.* (citing ERISA § 413(2)).

[127] 29 U.S.C. § 1104(c)(1)(A).

[128] *Tibble III* (quoting 29 C.F.R. § 2550.404c-1(d)(2)).

[129] *Id.*

[130] *Id.*

> requiring it to "(3) make certain that reliance on the expert's advice is reasonably justified under the circumstances." *Id.*[131]

The court thus concluded with a strong statement about what fiduciaries must do to demonstrate reasonable behavior when they are afforded deference.

Requests for *en banc* or Supreme Court review may follow, but in the meantime, *Tibble* is a significant decision with nuggets for both plaintiffs and defendants.

Abbott v. Lockheed Martin Corp., Nos. 12-3736, 12-8037 (7th Cir.)

Following a remand of class certification from the Seventh Circuit with instructions to "be guided by [the Seventh Circuit's] decisions in *Spano v. The Boeing Co.*, 633 F.3d 574, [50 EBC 1801] (7th Cir. 2011), and *Howell v. Motorola, Inc.*, 633 F.3d 552, [50 EBC 1865] (7th Cir. 2011)," the district court granted in part and denied in part plaintiffs' renewed motion for class certification on Sept. 24, 2012.[132] As described in the latest opinion, the *Abbott* court previously trimmed plaintiffs' claims down to the following:

> (1) whether excessive fees paid by the Plans provide a basis for Plaintiffs' fiduciary breach claim; (2) whether the Stable Value Fund (SVF) was properly disclosed to plan participants and was a prudent investment option for them; and (3) whether the Company Stock Funds (CSF) were a prudent investment option for plan participants.[133]

On the excessive fee claim, the *Abbott* court held that "a plan-wide class is warranted because the claimed excessive fees were imposed on all participants uniformly, as opposed to being charged on a fund-specific basis," carefully noting that such fees did not include revenue sharing.[134] The court found certification under Rule 23(b)(1)(A) and (B) appropriate. Certification of the excessive fee class follows *Spano*'s typicality holding, as outlined by the *Abbott* court:

> In *Spano*, the Seventh Circuit explained that determining whether a plan-wide class is suitable depends on whether fees are "fund-specific," in which case a plan-wide class would be inappropriate, or "imposed equally on every plan participant," in which case a plan-wide class would be warranted. [*Spano v. The Boeing Co.*, 633 F.3d 574, 590 (7th Cir. 2011)]. The court emphasized that "[p]recision on this point is essential to ensure that the class representative's claim is typical." *Id.*[135]

The *Abbott* opinion does not address whether a fund-specific fee claim could be certified as a subclass, though it seems as if the judges are skeptical that it could be. *Spano* itself, though, suggests that subclassing is exactly what a court should do.

On the plaintiffs' SVF claim, the court denied certification on typicality grounds, finding plaintiffs' attempt to divide up the proposed class into those who outperformed a benchmark and those who underperformed it was problematic. The court certified the company stock class.

The plaintiffs filed a Rule 23(f) petition and on Nov. 21, 2012, the Seventh Circuit again accepted review. The AARP sought leave to file an *amicus* brief, as have industry supporters.

Spano v. The Boeing Co. , No. 06-743 (S.D. Ill.)

Following the Seventh Circuit's decision remanding class certification,[136] plaintiffs in *Spano* filed an amended class certification motion on March 2, 2011, and their reply was filed in September of 2011. Defendants' motions for summary judgment were denied as premature on Sept. 19, 2012. Class certification is yet to be resolved.

Beesley v. Int'l Paper Co., No. 06-703 (S.D. Ill.)

Beesley was remanded after the *Spano* decision. In a Sept. 17, 2012 order on pending motions, the court denied some motions as stale and indicated it would hear the plaintiffs' renewed class certification motion, which was briefed in 2011.[137] According to the docket, settlement conferences were held on Oct. 5, 2012 and March 5, 2013, and more talks may be ordered.

Leimkuehler v. Am. United Life Ins. Co., No. 12-1081 (7th Cir.)

In *Leimkuehler v. American United Life Insurance Co.*, No. 10-0333 (S.D. Ind.),[138] the trustee of an ERISA plan sued the insurance company whose separate accounts were investment options for the plan. The district court granted summary judgment to the defendant. On June 1, 2012, DOL filed an amicus brief in support of the plaintiffs' appeal of that judgment, urging the Seventh Circuit Court of Appeals to reverse.[139]

Issues on appeal surround the defendant's fiduciary status—specifically, whether an insurance contract allowing the insurer to affect investment options and its own compensation after the contract is in place gives rise to fiduciary status, whether the defendant had "successfully contracted out of being a fiduciary," whether it was error to rely on *Hecker*, and whether supposed failure to "exercise" fiduciary authority by maintaining investments on an initial fund menu excuses a fiduciary from ERISA liability. The case involves claims for fiduciary breach and prohibited transactions. According to DOL, "[u]nder the logic of the district court's decision, an insurer, service provider, or trustee would have no fiduciary responsibility with respect to assets entrusted to its care and discretion, so long as it simply left the

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[131] *Id.*

[132] *Abbott v. Lockheed Martin Corp.*, 286 F.R.D. 388, 394 (S.D. Ill. 2012).

[133] *Id.*

[134] *Id.* at 396.

[135] *Id.* at 395-96.

[136] *Spano v. The Boeing Co.*, 633 F.3d 574, 50 EBC 1801 (7th Cir. 2011).

[137] *Beesley v. Int'l Paper Co.*, No. 06-0703 (S.D. Ill. Sept. 17, 2012).

[138] *Leimkuehler v. American United Life Insurance Co.*, No. 10-0333, 52 EBC 1001 (S.D. Ind. Jan. 5, 2012), *appeal docketed*, No. 12-1081 (7th Cir. Jan. 12, 2012).

[139] Brief of the Secretary of Labor as Amicus Curiae in Support of Plaintiff-Appellant Urging Reversal and Remand, *Leimkuehler v. Am. United Life Ins. Co.*, No. 12-1081 (7th Cir. June 1, 2012) (ECF No. 26).

assets in the same investment, no matter how expansive its contractual authority or imprudent the investment. This however, is not the law."[140]

The Seventh Circuit heard oral argument on Nov. 28, 2012, before Judges Michael S. Kanne, Diane P. Wood, and Diane S. Sykes.

Laboy v. Bd. of Trs., No. 12-3401 (2d Cir.)

Laboy is a class action by a participant in a plan asserting breach of fiduciary duty claims for excessive fees and imprudent selection of underperforming funds. In *Laboy v. Board of Trustees of Building Service 32 BJ SRSP*, No. 11-5127 (S.D.N.Y.) (*Laboy I*),[141] the district court contrasted the failed excessive fee claims in *Hecker*[142] with the successful pleading in *Braden*[143] and found the *Laboy* claims to be more similar to the former. The court criticized plaintiffs' lack of benchmarking comparisons and noted there were no allegations of self-dealing.[144] The court dismissed the claims and allowed plaintiff to replead.

In dismissing the second amended complaint with prejudice in *Laboy II*, the court held:

> Laboy's decision to move the excessive fee and expense allegations from their own independent claim in the [first amended complaint] and use them to supplement the claim for imprudence due to failure to monitor in the [second amended complaint] amounts to little more than cutting and pasting. For the reasons discussed in my earlier opinion, I find that these allegations are insufficient to state a claim for imprudent monitoring.[145]

The court again chided the plaintiff for failing to allege fund selection based on self-interest or clear incompetence. Relying on *Hecker* for the proposition that a particular "mix" of funds is not required by ERISA, the court found the plaintiff's failure to allege anything about the selection or monitoring process fatal to his claims. The court distinguished *Braden* at length and closed with this:

> As I explained in my earlier opinion, self-interest is the lynchpin for nearly every claim charging breach of fiduciary duty in the ERISA context. That lynchpin is absent from the [second amended complaint]. This is not to say that a fact pattern might state a claim based solely on allegations of incompetence, but rather that this is not such a case.[146]

So, while the court may have been harsh on the plaintiff for not alleging more about a process he had no access to observe, it is clear that he should have more clearly alleged poor fund selection, and it would have made all the difference if he could have alleged self-interested decisionmaking.

Defendants moved for attorneys' fees, which were denied.[147] Plaintiff appealed to the U.S. Court of appeals for the Second Circuit, the case was argued on Jan. 15, 2013, and a Summary Order and Judgment affirming dismissal was issued on March 6, 2013. Plaintiff may seek further review, but this case is probably over.

Ruppert v. Principal Life Ins. Co. , No. 11-2554 (8th Cir.)

The plaintiff in this class of plans case appealed final judgment and the district court's class certification denial to the Eighth Circuit. The case was argued on April 18, 2012, before Judges James B. Loken, Steve M. Colloton, and Bobby E. Shepherd. On Feb. 13, 2013, the court dismissed the appeal for lack of jurisdiction because (1) the consent judgment below left Ruppert's claims not finally resolved and (2) Ruppert's voluntary dismissal of his individual claims rendered the case moot, with no case or controversy left.[148] A mandate was issued on March 7, 2013. Like *Laboy*, this case is probably done.

Santomenno v. Transamerica Life Ins. Co., No. 12-2782 (C.D. Cal.)

This case is brought by plan participants on behalf of a class of plans that use Transamerica's group annuity contract platform to provide investment options in their 401(k) plans. The plaintiffs allege fiduciary breaches and prohibited transactions based on excessive fees charged in connection with Transamerica's separate accounts. Transamerica advised the plans that these investments are prudent and offers a "fiduciary warranty," among other things, yet disputed its fiduciary status. Defendants' motions to dismiss were briefed and argued in October of 2012. On Feb. 19, 2013, the District Court for the Central District of California denied Defendants' motions to dismiss as to all ERISA claims, finding that Transamerica could not contract its way out of fiduciary status or collect unreasonable fees after it became a fiduciary.[149] The opinion articulates well the consequences of a service provider's retention of discretion over its own fees and, separately, the power over an investment lineup: both result in fiduciary status.

On March 6, 2013, the defendants moved for an amendment of the court's motion to dismiss order to certify an interlocutory appeal pursuant to 28 U.S.C. § 1292(b).[150] On March 13, 2013, the defendants moved to strike the plaintiffs' class allegations.

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[140] *Id.* at 26.

[141] *Laboy v. Board of Trustees of Building Service 32 BJ SRSP*, No. 11-5127, 2012 BL 52945, 53 EBC 2171 (S.D.N.Y. Mar. 6, 2012) (*Laboy I*).

[142] *Hecker v. Deere & Co.*, 556 F.3d 575, 45 EBC 2761 (7th Cir. 2009).

[143] *Braden v. Wal-Mart Stores*, 588 F.3d 585, 48 EBC 1097 (8th Cir. 2009).

[144] *Laboy I*.

[145] *Laboy v. Bd. of Trs. of Bldg. Serv. 32 BJ SRSP*, No. 11-5127, 2012 BL 198316, 53 EBC 2773 (S.D.N.Y. Aug. 7, 2012) (*Laboy II*).

[146] *Id.*

[147] *Laboy v. Bd. of Trs. of Bldg. Serv. 32 BJ SRSP*, No. 11-5127, 2012 BL 293860 (S.D.N.Y. Nov. 8, 2012) (*Laboy III*).

[148] *Ruppert v. Principal Life Ins. Co.*, 705 F.3d 839 (8th Cir. 2013).

[149] *Santomenno v. Transamerica Life Ins. Co.*, No. 12-2782, 2013 BL 45042 (C.D. Cal. Feb. 19, 2013) (ECF No. 137).

[150] *See Santomenno v. Transamerica Life Ins. Co.*, No. 12-2782, Motion filed Mar. 6, 2013 (ECF No. 140).

Nolte v. CIGNA Corp., No. 07-2046 (C.D. Ill.)

In this case alleging conflicts of interest and excessive fees on separate account investment options, summary judgment and judgment on the pleadings motions have been suspended pending the court's class certification decision, a hearing about which was held on Oct. 20, 2011. On Jan. 25, 2013, defendant Prudential Retirement Insurance and Annuity Company filed its second petition for writ of mandamus seeking the Seventh Circuit's intervention and relief from the district court's ruling that the fiduciary exception to the attorney client privilege requires disclosure of certain documents. Prudential had requested a stay while the petition was pending. On Feb. 25, 2013, the Seventh Circuit denied the petition and the parties will now proceed with discovery.

In re Northrop Grumman Corp. ERISA Litig., No. 06-6213 (C.D. Cal.)

This case makes allegations of excessive fees on certain plan investment options and was filed by participants in the Northrop Grumman 401(k) plan. After Judge Manuel L. Real denied class certification and the Ninth Circuit reversed, assigning the case to a new judge (Margaret M. Morrow), a Rule 23(b)(1) class was certified on March 29, 2011, and summary judgment was briefed in 2011, with supplemental authorities submitted in 2012 and in early 2013. The motions remain pending.

Leber v. Citigroup, Inc., No. 07-9329 (S.D.N.Y.)

Leber v. Citigroup involved claims by two plan participants for prohibited transactions and fiduciary breaches arising out of the selection of mutual fund options for their plan. On defendants' motion to dismiss, only one prudence claim survived, alleging imprudence for "steering Plan assets to Citigroup affiliated mutual funds with higher investment advisory fees than those of competing funds."[151] Plaintiffs' prohibited transaction and ERISA Section 502(a)(3) claims were dismissed. In a subsequent ruling, the district court granted in part plaintiffs' motion for leave to amend their excessive fee lawsuit.[152] Summary judgment was briefed in early 2012, and plaintiffs filed another motion to amend in April of 2012. Both remain pending.

Diebold v. N. Trust Invs., N.A., No. 09-1934 (N.D. Ill.)

In this securities lending case brought by plan participants on behalf of a class of plans, plaintiffs allege excessive fees and prohibited transactions against plan fiduciaries, charging that they set and took unreasonable compensation for securities lending services. In allowing plaintiffs to amend, the court held that "ERISA requires reasonable compensation arrangements between fiduciaries and plans, and 'a fiduciary's contract with an employer cannot get it off the hook with the employees who participate in the ERISA plan.' *IT Corp. v. General Am. Life Ins. Co.*, 107 F.3d 1415, 1418 (9th Cir.1997); *see* 29 U.S.C. § 1108(b)(2), (6), (8)."[153] The court also rejected the defendants' arguments that listing fees in agreements with the plans was sufficient to "impute actual knowledge on the individual Plaintiffs."[154] The court allowed a Section 406(a) prohibited transaction amendment but denied the amendment request as to Section 406(b). Plaintiffs' class certification motion was briefed and is pending.

Golden Star, Inc. v. Mass Mutual Life Ins. Co., No. 11-30235 (D. Mass.)

The complaint in *Golden Star* alleges breach of fiduciary duties and prohibited transactions by a plan service provider in connection with revenue sharing receipts. The plaintiff's motion for class certification is set to be briefed by March of 2013.

Cases Filed in 2012

There are several cases to watch with no significant activity as of early 2013.

- *Butler Nat'l Corp. v. Union Central Life Ins. Co., No. 12-177 (S.D. Ohio)*: A separate account case brought by a fiduciary/plan administrator on behalf of a class of plans, challenging "pay-to-play" revenue sharing kickback arrangements orchestrated by Union Central.
- *Pueblo of Laguna Ret. Comm. v. Metlife Ins. Co. of Conn., No. 12-555 (D.N.M.)*: A (non-class) case involving annuity contracts that allegedly charged excessive fees to the plans.
- *Stargel v. SunTrust Banks, Inc., No. 12-3822 (N.D. Ga.)*: A class action by participants in the Sun Trust 401(k) plan alleging excessive fees and imprudent investment in affiliated funds. A motion to dismiss the amended complaint is pending on statute of limitations issues similar to those addressed in *Tibble* and *David*.

Tussey Spin-Offs. . .

While 2012 started with the landmark decision in *Tussey*, 2013 may be the year of the *Tussey* spin-off case and widespread liability for Fidelity as to the multitude of 401(k) plans to which it provides services and investment products. At least three cases have been filed to date seeking to capitalize on the holdings in *Tussey* regarding Fidelity's retention of float in violation of ERISA. With *Tussey* on appeal, however, these lawsuit may soon be on hold pending the Eighth Circuit's resolution of *Tussey*:

- *Kelley v. Fid. Mgmt. & Trust Co., No. 13-10222 (D. Mass.)*: A class of plans case seeking to cinch widespread liability for Fidelity's retention of float building on the plaintiffs' victory in the plan specific holdings of *Tussey*.

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151 *Leber v. Citigroup, Inc.*, No. 07-9329, 2010 BL 55992, 48 EBC 2418 (S.D.N.Y. Mar. 16, 2010) (*Leber I*).

152 *Leber v. Citigroup, Inc.*, No. 07-9329, 2011 BL 286782, 52 EBC 1845 (S.D.N.Y. Nov. 8, 2011) (*Leber II*).

153 *Diebold v. N. Trust Invs., N.A.*, No. 09-1934 (N.D. Ill. Sept. 10, 2012) (ECF No. 164).

154 *Id.*

- *Boudreau v. Fid. Mgmt. & Trust Co., No. 13-10524 (D. Mass.)*: Just filed in the District of Massachusetts on a similar theory as *Kelley*.
- *Columbia Air Services, Inc. v. Fid. Mgmt. & Trust Co., No. 13-10222 (D. Mass)*: The first *Tussey* spin-off to be filed by a plan fiduciary plaintiff.

Conclusion

Fee litigation surged in development in 2012 and early 2013, and with even more cases poised for resolution of important motions at both the district court and appellate levels, the rest of 2013 likely will be eventful.

Outcomes in 2012—particularly in *Tussey*, *Krueger*, *HSI*, and *Borroughs*—demonstrate the overarching themes:

- A prudent process must include benchmarking and the reduction of fee structures to dollars collected for a proper analysis.
- Plans must use the bargaining power they have to get better deals on fees, secure rebates, and include cheaper share classes.
- Fiduciaries cannot use their control over plans or plan assets to benefit themselves or their corporate interests or to make their proprietary products more marketable.
- Retention of benefits (such as income on float) or distribution outside an ERISA plan is forbidden.
- Having hundreds or thousands of investment options cannot insulate a plan's fiduciaries from liability.
- Having control over ones own fees or control over a plan investment lineup (including the ability to change, add, or remove options) confers fiduciary status on service providers, who cannot contract their way out of fiduciary status.
- Insurance company separate account products, which often include wrappers and significant add-on fees, will face greater scrutiny on the heels of rulings that the service providers offering these platforms are fiduciaries with respect to their compensation.
- Class of plans cases are certifiable under Rule 23(b)(3).
- Hiding fees leads to ERISA liability, particularly by service providers who set their own compensation and thereby assume fiduciary status.
- Non-fiduciaries who participate in fiduciary breaches and prohibited transactions face liability under ERISA § 502(a)(3).

The fact patterns that make a good case will continue to emerge as the cases on court dockets across the United States are tested by defendants and judges in 2013. Additionally, while potential claims flowing directly from service providers' violations of the Section 408(b)(2) disclosure rules may take another year to surface, claims for past fiduciary breaches and prohibited transactions brought to light in recent months by way of the disclosures provided under the Section 408(b)(2) regulations are ripe for litigation now and may soon hit the courts.[155]

What's clear is that fee litigants are breaking new ground by shining a spotlight on a broad array of fee structures and practices that have long been accepted as the status quo in the retirement services industry, and they are winning a fair number of their litigation battles. Not only that, court opinions are pushing the jurisprudence forward and recognizing both ERISA's broad protections and the diverse conduct that can constitute fiduciary breaches and prohibited transactions in the context of 401(k) plan fees.

[155] *See* Obrist, "ERISA Fee Litigation: The Impact of New Disclosure Rules, and What's Next in Pending Cases," *supra* note 12.