Bloomberg BNA

Pension & Benefits Daily ™

ERISA Fee Litigation: The Impact of New Disclosure Rules, and What's Next in Pending Cases

BY GRETCHEN S. OBRIST

Employee Retirement Income Security Act fee litigation has flourished recently. Developed during the past decade, this body of cases challenges the fees that are paid by participants out of plan assets in defined contribution plans or collected by tax code Section 401(k) plan service providers that profit from their relationships with ERISA plans. Both direct and indirect fees that service providers collect impact the overall cost of investment options to participants. Transparency around indirect fees has been particularly lacking. In addition, because fiduciaries or service providers often include their own proprietary investment products in the Section 401(k) plans they run, conflicts of interest, which may be hidden from participants, are apt to keep fees high.[1]

Why do fees matter? More than *$3 trillion* in assets sit in participant-directed plans, and these plans have an estimated 72 million participants.[2] 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[3]) and 1.50 percent (150 basis points)—reduces total retirement savings by *more than a quarter*.[4] Because this impact on plan participants is so clear, many of the retirement services industry's longstanding practices are no longer being tolerated by astute participants and plan fiduciaries.

Now, with a store of pending cases on court dockets all over the country, and amid a new regulatory landscape, 2013 promises to be a big year in the development of the nascent jurisprudence of ERISA fee litigation. Cases already on file will continue to shape the legal theories and fact patterns that define what makes a good case. Also, new revelations about fees and conflicts of interest that have lurked in the shadows of the retirement plan services industry for many years will fuel more litigation. Together, these forces should further rein in 401(k) plan fees and increase transparency around fee arrangements, but it is going to be a long haul.

Background and Recent Developments

Three Common Kinds of Wrongdoing. 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—unbenchmarked, underperforming, expensive investment options with 12b-1, and other fees, excessive or unchecked revenue sharing, and/or other unnecessary or uncalculated (and thus unmonitored) fees.

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

Gretchen S. Obrist (gobrist@kellerrohrback.com) is a member of the complex litigation group at Keller Rohrback in Seattle, with a practice emphasis on class action litigation of ERISA and consumer protection claims.

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

[2] *See* Department of Labor, Employee Benefits Security Administration, *Fact Sheet, Final Rule to Improve Transparency of Fees and Expenses to Workers in 401(k)-Type Retirement Plans* (Feb. 2012), http://www.dol.gov/ebsa/newsroom/fsparticipantfeerule.html.

[3] 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, 50 basis points equals 0.50 percent.

[4] Department of Labor, EBSA, *A Look at 401(k) Plan Fees* (Oct. 2010), http://www.dol.gov/ebsa/publications/401k_employee.html.

■ 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.

Recent Decisions. Court decisions in fee litigation during the past year confirm that conflicts of interest, kickbacks, self-dealing, and 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. A few highlights from 2012—each in a different procedural posture—demonstrate the trends:

■ ***Tussey v. ABB Inc.***[5] Following a bench trial in 2010, the court awarded damages of nearly $37 million plus injunctive relief, fees, and costs—together totaling more than $50 million—against plan sponsor ABB and trustee/recordkeeper Fidelity. Key liability findings centered on ABB's use of the plan to subsidize its own corporate costs, ABB's lack of benchmarking to assess the reasonableness of revenue sharing, and Fidelity's use of plan assets to benefit itself and mutual fund shareholders by retention and extra-plan distribution of ''float,'' which is interest income generated on funds sitting in accounts used to facilitate various plan transactions.

■ ***Krueger v. Ameriprise.***[6] Here, a fiduciary included proprietary funds in an investment lineup, used an ERISA plan to increase the marketability of those funds to the outside world, and imposed an excessive fee-generating fund transfer structure. In denying Ameriprise's motion to dismiss, the court made two things clear. 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 v. Deere & Co.*, which affirmed the dismissal of claims against a plan with hundreds of investment options.[7] 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.

■ ***Healthcare Strategies Inc. v. ING Life Ins. & Annuity Co.***[8] A class of plans was certified under Rule 23(b)(3) in this case brought by an ERISA fiduciary (a plan administrator) challenging ILIAC's fees collected in connection with the separate account investment options that ILIAC offered to thousands of 401(k) plans. Specifically, HSI alleges ILIAC's fiduciary status through control over plan assets and challenges ILIAC's extraction of revenue-sharing payments from mutual funds in exchange for their inclusion in plan menus. The court's certification order confirmed that fee structures associated with insurance companies' separate account platforms are ripe for scrutiny and the fiduciaries that control those fees must abide by ERISA.

■ ***Borroughs Corp. v. Blue Cross Shield of Michigan.***[9] Plaintiffs—the plan sponsor and a welfare plan—alleged that Blue Cross set its own fees and then hid them, failing to provide accurate fee information on statements. The court granted summary judgment to the plaintiffs on their ERISA prohibited transaction claim—setting the stage for future analysis of hidden fees under ERISA.

A slew of other cases developed in 2012,[10] and even more are likely to have significant activity in 2013.[11]

Given the number of cases that remain unresolved in the district courts or currently are up on appeal, outcomes in already-filed lawsuits will continue to shape the fee litigation landscape significantly. But developments will not end there. DOL's recent push for increased transparency is almost sure to result in more litigation and further development in this niche of ERISA law.

Outlook for New Fee Litigation in 2013

In promulgating new regulations requiring fuller disclosures and bringing rigorous reasonableness assessments to the forefront of plan sponsors' fiduciary responsibilities, DOL has targeted many of the fee opacity problems and conflicts of interest that have been central to recent fee litigation. With these regulations now in place—requiring increased disclosure from service providers to plan fiduciaries,[12] and from plan sponsors to participants[13]—a lot of new information about fees is ostensibly becoming available to would-be fee litigants.

As these new fee disclosures roll out, significant revelations about fees that service providers have been

---

[5] No. 06-4305, 2012 BL 84927, 52 EBC 2826 (W.D. Mo. Mar. 31, 2012)(63 PBD, 4/3/12; 39 BPR 697, 4/10/12).

[6] No. 11-02781, 2012 BL 313619 (D. Minn. Nov. 20, 2012)(227 PBD, 11/28/12; 39 BPR 2310, 12/4/12).

[7] 556 F.3d 575, 586, 45 EBC 2761 (7th Cir. 2009)(28 PBD, 2/13/09; 36 BPR 357, 2/17/09).

[8] No. 11-282, slip op., (D. Conn. Sept. 26, 2012), ECF No. 126.

[9] Nos. 11-12565 & 11-12557, 2012 BL 232703, 53 EBC 2829 (E.D. Mich. Sept. 7, 2012)(175 PBD, 9/11/12; 39 BPR 1761, 9/18/12).

[10] *See, e.g.*, *Nationwide Life Ins. Co. v. Haddock*, 2012 BL 28710, 52 EBC 1161 (2d Cir. 2012)(24 PBD, 2/7/12; 39 BPR 306, 2/14/12)(remanding class of plans case challenging revenue sharing associated with separate accounts for consideration of certification under Rule 23(b)(3)); *Glass Dimensions Inc. v. State Street Bank & Trust Co.*, 285 F.R.D. 169 (D. Mass. 2012)(certifying class of plans alleging that collective trust manager fiduciaries set and collected excessive and unreasonable compensation for themselves); *National Security Systems Inc. v. Iola*, 700 F.3d 65 (3rd Cir. 2012)(218 PBD, 11/13/12; 39 BPR 2220, 11/20/12)(finding nonfiduciary liable under ERISA Section 502(a)(3) for participating in prohibited transactions in connection with hidden kickbacks); *Santomenno v. John Hancock Life Ins. Co.*, 677 F.3d 178, 52 EBC 2807 (3d Cir. 2012)(73 PBD, 4/17/12; 39 BPR 791, 4/24/12), *cert. denied*, 133 S. Ct. 529 (2012)(210 PBD, 10/31/12; 39 BPR 2102, 11/6/12)(holding that plaintiffs bringing excessive fee claims did not have to make presuit demand or join trustees).

[11] *See infra*, Pending Cases to Watch in 2013.

[12] *See* 29 C.F.R. § 2550.408b-2 (2012) (the ''408(b)(2) regulation,'' published in final form at 77 Fed. Reg. 5,632 (Feb. 3, 2012)).

[13] *See* 29 C.F.R. § 2550.404a-5 (2011) (the ''404(a) regulation,'' published in final form at 75 Fed. Reg. 64,910 (Oct. 20, 2010)).

charging, but hiding, for many years will no doubt come to light (and many already have). Associated legal challenges to newly revealed fees and conflicts of interest are likely to abound. These challenges could come from plan fiduciaries or participants, and will be a rude awakening to fiduciary service providers that have been hiding their fees.

Aside from uncovering past hidden fees that already are actionable as breaches of loyalty and/or prohibited transactions, the new rules may instigate novel and untested fee structures (or obfuscations), designed by service providers that must operate in the new disclosure regime but still want to keep some information to themselves (or at least keep it difficult to figure out). If these changes involve any of the hallmarks of what currently makes a good fee case—self-interest, lack of oversight, and kickbacks—fee litigation is likely to persist, and easily could increase, under the new regulatory scheme. That is, if somebody figures it out.

Going forward, plan fiduciaries must enforce prohibited transaction regulations against service providers or face liability themselves. Plan sponsors have the responsibility to (1) monitor and benchmark fees for reasonableness; (2) identify conflicts of interest; (3) make sure service provider disclosures are full and accurate (and fire the service provider if disclosures are not forthcoming);[14] and (4) make sure participant disclosures are accurate and effective. Fiduciary decision-makers that turn a blind eye to fees or fail to investigate them will be in the hot seat.

Are Prohibited Transaction 408(b)(2) Disclosures Helpful or Opaque? The Government Accountability Office released a report in April 2012 revealing the extent to which plan sponsors—particularly of small- and medium-sized plans—are unaware of the fees paid to plan service providers from participant accounts or by mutual fund companies.[15] For example, many plan sponsors do not know if there is revenue sharing associated with investment options or do not understand its impact.[16] About half of plan sponsors interviewed did not know if they or their participants paid investment management fees, or they incorrectly thought these fees were waived—despite the fact that investment management fees account for a majority of 401(k) plan fees.[17] In addition, 82 percent of plan sponsors had never asked about sub-TA fees,[18] and 95 percent of them had not asked service providers for information regarding transaction or trading costs.[19] The GAO also reported that insurance products—*i.e.*, group annuity contracts and separate account platforms—are particularly difficult for plan sponsors to evaluate and can be packed with hidden fees.[20] Given this landscape, well-done Section 408(b)(2) disclosures to fiduciaries equipped to understand the information they receive could provide a wake-up call to plan fiduciaries and, in turn, drastically reduce plan fees.

One goal of the disclosure rules plainly is to lower fees. Some evidence suggests that, in advance of the disclosure deadline, many service providers did reduce their fees—or appeared to do so. But are the fees really lower? A survey by NEPC LLC—itself a consulting service provider to defined contribution plans—suggests that, while recordkeeping fees fell by 11 percent in 2012, overall expense ratios fell by only 2 percent, perhaps because bundled service providers are simply ''shifting fees to one part of the business from another; for instance, accepting lower administrative revenues on one side but seeking higher investment management revenues on the other.''[21]

The word on the street is that many of the new plan service provider disclosures do not seem to be revealing very much. Perhaps plan fiduciaries/sponsors do not know what to look for—or what they are looking at. Or have service providers figured out a way to keep their fees fuzzy? A recent article suggests that undisclosed amounts likely still are lurking—dubbed ''enhanced revenue'' or undisclosed ''backdoor'' fees.[22]

According to independent fiduciary consultants Mark D. Mensack and Louis S. Harvey of Dalbar Inc., the service provider disclosures first made in fall 2012 are of three varieties: ''spirit of the law,'' ''letter of the law,'' and ''business as usual or needle in the haystack.''[23] ''Spirit of the law'' disclosures are the most clear and understandable. The ''letter of the law'' disclosures consolidate information into a single document, but still leave it up to plan sponsors to ''navigate the legal and technical language to assess reasonableness.''[24] ''Needle in the haystack'' disclosures force plan sponsors to wade through a ''number of references, prospectuses, websites, plan documents, etc.,'' to ''search for answers.''[25]

Others agree that many disclosures remain opaque. According to an article in Bloomberg BNA's *Pension & Benefits Daily*, service provider disclosures to date are ''not 'maps to clarity.' ''[26] They are often confusing, directing participants and sponsors to websites or providing complicated formulas for participants to try and fig-

[14] If disclosures are not adequate, and if additional information is not provided within 90 days of a fiduciary's request, fiduciaries must report to DOL and fire their service providers or be held responsible for participating in prohibited transactions. 29 C.F.R. § 2550.408b-2(c)(1)(ix)(F-G).

[15] U.S. Gov't Accountability Office, GAO-12-325, *401(k) Plans: Increased Educational Outreach and Broader Oversight May Help Reduce Plan Fees* (April 2012), http://www.gao.gov/assets/600/590359.pdf.

[16] *Id.* at 24-28.

[17] *Id.* at 17-18.

[18] *Id.* at 18. 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.

[19] *Id.* at 35.

[20] *Id.* at 29-34.

[21] Ross Bremen and Matthew Rowell, *Defined Contribution Plan Fees Hit a Record Low: NEPC Study* (Dec. 2012), http://www.nepc.com/research/110-defined_contribution_plan_fees_hit_a_record_low_nepc_study.

[22] Florence Olsen, ''DOL Looking at Sample Documents to Assess Compliance with 408(b)(2) Fee Disclosures,'' *Pension & Benefits Daily*, Bloomberg BNA (216 PBD, 11/8/12; 39 BPR 2131, 11/13/12).

[23] Mark Mensack, *Rule 408(b)(2): The New Fiduciary Paradox*, http://www.prudentchampion.com/wp-content/uploads/2012/08/Rule408b2-The-New-Fiduciary-Paradox-7-30-12.pdf.

[24] *Id.* at 4.

[25] *Id.*

[26] Andrea L. Ben-Yosef, ''Disclosure Rules Give Fiduciaries New Obligations but Same Core Duties,'' *Pension & Benefits Daily*, Bloomberg BNA (237 PBD, 12/12/12; 39 BPR 2390, 12/18/12).

ure out.[27] Some disclosures are far from simple one-pagers—instead they are found in a collection of lengthy documents, such as ''five 20-page documents that were very confusing.''[28] The nature of the disclosures has led to calls for a single-page disclosure—either voluntarily or at the direction of DOL. For example, one consultant advocates that plan sponsors ''return any confusing 'disclosures' to service providers as 'noncompliant' '' and that they then ''provide their own single page disclosure'' asking for a series of simple data points, with one form for each provider (multiple forms required for bundled service providers), multiple choice questions, and straightforward fee information expressed in dollars and basis points.[29]

Plan sponsors could be on the hook—and outside DOL's ''reasonable belief'' safe harbor—if they fail to follow up on incomplete disclosures or simply rely on service providers' assurances that all indirect compensation has been disclosed. If it has not, it is a prohibited transaction, and if it has, it must be determined to be reasonable by benchmarking and other evaluations. Moreover, service providers will be participating in prohibited transactions with ERISA plans—regardless of whether they are fiduciaries—if they fail to adequately disclose their fees. The lack of a ''reasonable belief'' exception for vendors—as is provided to plan fiduciaries—prompted some to ask DOL to implement a safe harbor for errant plan service providers.[30] Even if such an exception is granted for good-faith mistakes, service providers that knowingly hide the ball will face liability.

The purpose of the new rules is to provide plan fiduciaries with enough information to determine whether compensation to service providers is reasonable (and to satisfy their 404(a) prudence and loyalty obligations), to identify potential conflicts of interest, and to satisfactorily report and disclose fees to participants. It is far from clear that this purpose is being served.

How Good Are the 404(a) Disclosures? As has long been true, plan participants often do not know about or understand 401(k) plan fees. According to a recent study by AARP, 71 percent of plan participants ''reported that they did not pay any fees'' for their 401(k) plan.[31] According to the survey, ''[w]hen respondents were told that financial services companies that manage 401(k) plans charge fees for administering and managing those plans, and that the fees are paid by the employer and/or the employees that participate in the plan, about three in five (62 percent) reported that they did not know how much they were paying in fees and expenses for their 401(k) plan.''[32]

Without basic knowledge and understanding about fees, participants' savings will suffer. A study by a trio of finance professors concludes that, when presented with a plan lineup in which the deck has been stacked toward proprietary funds, participants are extremely unlikely to undo proprietary favoritism, resulting in investment in more expensive and underperforming funds, to the disproportionate benefit of the sponsor or service provider whose affiliated funds are on the menu.[33] Given these results, it is critically important for plan fiduciaries to keep a watch out for favoritism that depletes retirement savings. Fiduciaries' disclosures to participants about what is really happening with fees—and who is benefiting from their investments—must be clear, if they are to have any chance of efficacy. But with fiduciaries' own lack of knowledge on these matters demonstrated by the GAO's survey of plan sponsors, it is no surprise that opacity is vertical, leaving plan participants doubly in the dark when the fiduciaries of their plans do not really know what is going on (or are themselves beneficiaries of proprietary favoritism with little incentive to make that fact known).

A recent survey by the Plan Sponsor Council of America announced ''little impact'' on participant behavior after the first Section 408(b)(2) and 404(a) disclosures under the new regulatory regime.[34] Service providers and fiduciaries might like to pat themselves on the back for a job well done, but it could just be that participants continue to find the disclosures opaque and difficult to understand. Or perhaps the Section 404(a) disclosures do not say enough. For example, neither the many fees from revenue sharing, nor the 12b-1 fees that flow to service providers, have to be broken down for participants even under the new rules, because they are not considered to be separate from the expense ratio on a particular investment option. In the case of sub-TA fees that are not paid out of participant accounts, unaware participants will not understand that such fees (paid by somebody else) may create a windfall to service providers and that the fees participants actually are paying from their plan accounts should be lower when all fees collected by the service providers are taken into account.

So, perhaps the participant-level ''non-event'' has been driven by the service providers' failure to perform adequately and/or plan fiduciaries' failure to cut through the smoke and make fees understandable—particularly when they themselves benefit in some way from fee arrangements. Regardless of the reason, more time and education is needed to evaluate the big picture—including how much participants and their plan sponsors truly understand, as well as how much useful information plan sponsors are disclosing in an understandable fashion. In the meantime, fiduciaries on

[27] *Id.*

[28] Christopher Carosa, ''401k Fee Disclosure: What 6 Months Tells Us,'' *Fiduciary News* (Dec. 11, 2012), http://fiduciarynews.com/2012/12/401k-fee-disclosure-what-6-months-tells-us/.

[29] Christopher Carosa, ''Time Again for 401(k) Sponsors To Take a Stand,'' *BenefitsPro* (Dec, 27, 2012), http://www.benefitspro.com/2012/12/27/time-again-for-401k-sponsors-to-take-a-stand.

[30] Rebecca Moore, ''Attorneys Ask for Service Provider 408(b)(2) Remedy,'' *Plansponsor* (Oct. 18, 2012), http://plansponsor.com/Attorneys_Ask_for_Service_Provider_408b2_Remedy.aspx.

[31] AARP, *401(k) Participants' Awareness and Understanding of Fees* (Feb. 2011), http://assets.aarp.org/rgcenter/econ/401k-fees-awareness-11.pdf.

[32] *Id.* at 6.

[33] Pool, et al., supra note 1, at 3-4, 23-27, 30.

[34] Plan Sponsor Council of America, *PSCA's Fee Disclosure Snapshot Survey Results* (Oct. 2012), http://www.psca.org/uploads/Research/fees/Fee_Disclosure_Snapshot_Results_FINAL.pdf. *See also* Kristen Ricaurte Knebel, ''Disclosures Get Little Participant Attention, E-Communication May Help, Groups Say,'' *Pension & Benefits Daily*, Bloomberg BNA (218 PBD, 11/13/12; 39 BPR 2185, 11/20/12)(describing the effect of the new disclosures as a ''nonevent'').

the plan side should not let service providers write Section 404(a) participant disclosures unchecked—particularly if they are the same service providers with their own Section 408(b)(2) disclosure obligations to the plan. A plan service provider who hides or obfuscates its own fees in Section 408(b)(2) disclosures will be incapable of writing straightforward Section 404(a) disclosures for the plan to distribute to participants, thus exacerbating any opacity problem. Plan sponsors whose vendors or service providers ''handle[] it all'' are apparently prolific—but they are at risk.[35]

Savvy participants who get disclosures that suggest something is not right may be propelled to take legal action, as many already have. However, given what is known about how little participants and sponsors understand, the number of hidden problems—which must be uncovered before litigation is even a possibility—is likely very great.

Pending Cases to Watch in 2013

Whatever new litigation is filed on the heels of the new regulations, ongoing litigation will continue to shape the law and reveal the factual and theoretical hallmarks of a successful case. In this quickly developing field, it is unsurprising that a large number of cases and important issues remain unresolved. These are some cases to watch in 2013—some of which already have yielded important decisions this year.

David v. Alphin, **No. 11-2181 (4th Cir.):** The year 2013 started with the decision in *David v. Alphin*.[36] The Fourth Circuit affirmed summary judgment on the plaintiffs' fiduciary breach and prohibited transaction claims that 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.''[37] The court thus conflated initial selection with failure to remove, holding that all the claims, as the plaintiffs pleaded them, 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.''[38]

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.[39] 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.

Any petition for rehearing en banc is due by Feb. 28, so this may not be the end of the story.

Tibble v. Edison, **Nos. 10-56406, 10-56415 (9th Cir.):** *Tibble* involved 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 claim 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.[40] 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 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.''[41] The *Tibble* court also rejected the notion that utilization of an outside consultant absolves a fiduciary of any liability.[42] The court was equally unpersuaded by defendants' claims of mandatory investment minimums, holding that ''[t]he only way a fiduciary can obtain a waiver of the investment minimum is to call and ask for one.''[43]

The court entered judgment, awarding about $371,000 in damages to plaintiffs and ordering defendants to replace a retail share mutual fund with an institutional class share.[44] Plaintiffs have appealed to the extent that this judgment, the post-trial findings of fact and conclusions of law, and pretrial orders on summary judgment find in favor of defendants.

Both DOL and AARP filed amicus briefs in support of the plaintiffs-appellants. The case was argued Nov. 6, 2012, before Judges Alfred T. Goodwin, Diarmuid F.

[35] *See Mensack*, *supra* note 23 at 1.
[36] No. 11-2181, 2013 BL 10098 (4th Cir. Jan. 14, 2013).
[37] *Id.*
[38] *Id.*

[39] 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, 2013 BL 10098 (4th Cir. Dec. 28, 2011).
[40] *Tibble v. Edison International*, No. 07-5359, 49 EBC 1725 (C.D. Cal. July 8, 2010)(133 PBD, 7/14/10; 37 BPR 1560, 7/20/10).
[41] *Id.*
[42] *Id.*
[43] *Id.*
[44] *Id. See also Tibble v. Edison International*, No. 07-5359 (Dkt. Nos. 417, 418)(C.D. Cal. Aug. 9, 2010).

O'Scannlain, and Jack Zouhary. On Jan. 16, Edison submitted the Fourth Circuit's decision in *David v. Alphin*, No. 11-2181, 2013 BL 10098 (4th Cir. Jan. 14, 2013), as supplemental authority on the statute of limitations and prohibited transactions issues.

***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.[45] 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 the plaintiffs' fiduciary breach claim; (2) whether the stable value fund was properly disclosed to plan participants and was a prudent investment option for them; and (3) whether the company stock funds were a prudent investment option for plan participants.[46]

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.[47] 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 U.S. Court of Appeals for the Seventh Circuit explained that determining whether a planwide class is suitable depends on whether fees are ''fund-specific,'' in which case a planwide class would be inappropriate, or ''imposed equally on every plan participant,'' in which case a planwide class would be warranted.[48] The court emphasized that ''[p]recision on this point is essential to ensure that the class representative's claim is typical.''[49]

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.[50] The court certified the company stock class.[51]

The plaintiffs filed a Rule 23(f) petition and on Nov. 21, 2012, the Seventh Circuit again accepted review. Briefing is underway, AARP has sought leave to file an *amicus* brief, and a settlement conference is scheduled for March 21.

***Spano v. Boeing Co.*, No. 06-743 (S.D. Ill.):** Following the Seventh Circuit's decision remanding class certification, plaintiffs in *Spano* filed an amended class certification motion on March 2, 2011, and their reply was filed in September 2011. The defendants' motions for summary judgment were denied as premature on Sept. 19, 2012, and the class certification motion remains pending.

***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.[52] According to the docket, a settlement conference was held Oct. 5, 2012 (Dkt. No. 533), and another one is scheduled for March 5, 2013.

***Leimkuehler v. Am. United Life Ins. Co.*, No. 12-1081 (7th Cir.):** In *Leimkuehler v. American United Life Insurance Co.*, No. 10-0333, 2012 BL 2812, 52 EBC 1001 (S.D. Ind. Jan. 5, 2012)(4 PBD, 1/9/12; 39 BPR 62, 1/10/12), *appeal docketed*, No. 12-1081 (7th Cir. Jan. 12, 2012), 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 to reverse.

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 assets in the same investment, no matter how expansive its contractual authority or imprudent the investment. This however, is not the law.''[53]

The Seventh Circuit heard oral argument 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*,[54] the district court contrasted the failed excessive fee claims in *Hecker*[55] with the successful pleading in *Braden*[56] and found the *Laboy* claims to be more similar to the

[45] *Abbott v. Lockheed Martin Corp.*, 286 F.R.D. 388, 394, 53 EBC 2889 (S.D. Ill. 2012)(186 PBD, 9/26/12; 39 BPR 1872, 10/2/12).

[46] *Id.*

[47] *Id.* at 396.

[48] 633 F.3d at 590.

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

[50] *Id.* at 398-400.

[51] *Id.* at 400-04.

[52] *Beesley v. Int'l Paper Co.*, No. 06-0703 (Dkt. No. 528)(S.D. Ill. Sept. 17, 2012).

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

[54] No. 11-5127, 2012 BL 52945, 53 EBC 2171 (S.D.N.Y. Mar. 6, 2012)(45 PBD, 3/8/12; 39 BPR 500, 3/13/12)(*Laboy I*).

[55] *Hecker v. Deere & Co.*, 556 F.3d 575, 586, 45 EBC 2761 (7th Cir. 2009)(28 PBD, 2/13/09; 36 BPR 357, 2/17/09).

[56] *Braden v. Wal-Mart Stores*, 588 F.3d 585, 48 EBC 1097 (8th Cir. 2009)(226 PBD, 11/30/09; 36 BPR 2743, 12/1/09).

former. The court criticized plaintiffs' lack of benchmarking comparisons and noted there were no allegations of self-dealing.[57] The court dismissed the claims and allowed plaintiff to replead.

In dismissing the second amended complaint with prejudice, the court held that:

> Laboy's decision to move the excessive fee and expense allegations from its 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.[58]

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 linchpin for nearly every claim charging breach of fiduciary duty in the ERISA context. That linchpin is absent from the SAC. 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.[59]

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.[60] Plaintiff appealed to the U.S. Court of Appeals for the Second Circuit, and the case was argued Jan. 15.

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, Steven M. Colloton, and Bobby E. Shepherd. On Feb. 13, 2013, the appeals 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.[61]

Santomenno v. Transamerica Life Ins. Co., **No. 12-2782 (C.D. Cal.):** This case was 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 alleged fiduciary breaches and prohibited transactions based on excessive fees charged in connection with Transamerica's separate accounts. Transamerica advised the plans that these investments were prudent and offered a ''fiduciary warranty,'' among other things, yet disputed its fiduciary status. Defendants' motions to dismiss were briefed and argued in October 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. 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.[62]

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 were 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 Co. 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 also requested a stay while the petition is pending.

In re Northrop Grumman Corp. ERISA Litig., **No. 06-6213 (C.D. Cal.):** This case made 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 U.S. Court of Appeals for the Ninth Circuit reversed, assigning the case to a new judge, a Rule 23(b)(1) class was certified March 29, 2011, and summary judgment was briefed in 2011, with supplemental authorities submitted in 2012. The motion remains 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 the 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.''[63] Plaintiffs' prohibited transaction and ERISA Section 502(a)(3) claims were dismissed.[64] In a subsequent ruling, the district court granted in part the plaintiffs' motion for leave to amend their excessive-fee lawsuit. Summary judgment was briefed in early 2012, and plaintiffs filed another motion to amend in April 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, the plaintiffs alleged excessive fees and prohibited transactions against plan fidu-

---

[57] *Laboy I*, 2012 BL 52945, 53 EBC 2171.

[58] *Laboy v. Board of Trustees of Building Service 32 BJ SRSP*, No. 11-5127, 2012 BL 198316, 53 EBC 2773 (S.D.N.Y. Aug. 7, 2012)(155 PBD, 8/13/12; 39 BPR 1551, 8/14/12)(*Laboy II*).

[59] *Id.*

[60] *Laboy v. Bd. of Trs. of Bldg. Serv. 32 BJ SRSP*, No. 11-5127, 2012 BL 293860 (S.D.N.Y. Nov. 8, 2012)(219 PBD, 11/14/12)(*Laboy III*).

[61] *Ruppert v. Principal Life Ins. Co.*, No. 11-2554, 2013 BL 38178 (8th Cir. Feb. 13, 2013)(31 PBD, 2/14/13; 40 BPR 424, 2/19/13).

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

[63] *Leber v. Citigroup Inc.*, No. 07-9329, 2010 BL 55992, 48 EBC 2418 (S.D.N.Y. Mar. 16, 2010)(51 PBD, 3/18/10; 37 BPR 629, 3/23/10).

[64] *Leber v. Citigroup Inc.*, No. 07-9329, 2011 BL 286782, 52 EBC 1845 (S.D.N.Y. Nov. 8, 2011)(219 PBD, 11/14/11; 38 BPR 2107, 11/15/11).

ciaries, charging that they set and took unreasonable compensation for securities lending services. In allowing the 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, 20 EBC 2633 (9th Cir. 1997); *see* 29 U.S.C. § 1108(b)(2), (6), (8).''[65] 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.''[66] The court allowed a Section 406(a) prohibited transaction amendment but denied the amendment request as to Section 406(b). The 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* alleged 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 2013.

Newly Filed Cases. There are at least four newly filed cases to watch with no significant activity yet. Stay tuned.

- ***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 nonclass 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 is pending on statute of limitations issues similar to those addressed in *Tibble* and *David*.

- ***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*. With *Tussey* on appeal, however, *Kelley* may soon be on hold pending the Eighth Circuit's resolution.

Conclusion

Once the disclosure regulations have been in place for a while, it will become clear how many plan fiduciaries and service providers have opened themselves up to the new kind of ERISA fee litigation contemplated under DOL's prohibited transaction rules. However, while potential claims flowing from such violations 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 new regulations are ripe for litigation now.

In making their Section 408(b)(2) disclosures, some service providers have revealed that they have charged more than their contracts allowed or more than they disclosed in the past. The new rules should make concealing these fees (or proprietary biases that affect fees) more difficult, and if service providers come clean, plan fiduciaries may be shocked by what they learn. Both service providers and fiduciary decisionmakers that should have known better will be at risk. Faced with discoveries of hidden or unreasonable fees, many plan fiduciaries may decide to sue—following in the footsteps of the fiduciaries in cases like *HSI*, *Borroughs*, *Leimkuehler*, and others. If they do not sue, their plans' participants might, as in cases such as *Tussey*, *Kelley*, and *Krueger*.

Nonfiduciary service providers that participate in violations of ERISA in which plans are paying unreasonable fees or engaged in kickback schemes or self-dealing face as much liability risk now as ever, particularly given the scope of ERISA Section 502(a)(3) articulated in the *Iola* opinion.[67] However, self-dealing *fiduciary* service providers are at even greater risk with the new spotlight on fee transparency, given how easy it is for a vendor to jump from the category of ''just a service provider'' to being a fiduciary under ERISA's functional test. ERISA has always required fiduciary service providers to tell the truth about fees they take from plan assets—whether reasonable or not.

The distinct risk to fiduciary service providers is a function of ERISA's structure and purpose. The Section 408(b)(2) prohibited transaction regulations are supposed to help plan fiduciaries decide whether fees are reasonable for purposes of ERISA Section 406(a) (prohibited transactions involving a ''party in interest''). These regulations arise under ERISA Section 408(b)(2)—which is ERISA Section 406(a)'s reasonableness exception counterpart. Thus, previously hidden yet reasonable fees collected by ''just a service provider'' may not necessarily lead to liability. *But no reasonableness exception exists for ERISA Section 406(b) prohibited transactions committed by fiduciaries.* Significantly, the new regulations explicitly note that nothing in them relieves fiduciary service providers from the restrictions of ERISA sections 404 or 406(b).[68] Fiduciary breaches of loyalty, kickbacks, and self-dealing are actionable under existing ERISA law and carry liability entirely outside the new regulatory scheme. Therefore, fiduciary service providers that concealed even ''reasonable'' fees before the new prohibited transaction regulations were in place and that now are revealing for the first time the extent and amount of their previously hidden fees, may find themselves going to court in 2013, having spawned the next wave of ERISA fee litigation.

---

[65] *Diebold v. N. Trust Invs. N.A.*, No. 09-1934, 50 EBC 1508 (N.D. Ill. Sept. 10, 2012).

[66] *Id.*

[67] *See supra* note 10.

[68] *See* 75 Fed. Reg. 41600, 41613 n.12.

