# The War on Retirement Plan Fees: Is Anyone Safe?

Authored by: Alison L. Martin and Lars C. Golumbic

CHUBB®

GROOM LAW GROUP

# Fiduciaries of retirement plans of all sizes are being sued as the wave of excessive fee claims continues to grow. Could you be next?

Almost every employer that sponsors a retirement plan should be concerned about potential liability for a type of exposure known as excessive fee claims. Historically filed against only the largest organizations, an increasing number of smaller retirement plans have faced excessive fee litigation over the past couple of years. With this surge in litigation, it's important that all fiduciaries, regardless of plan size, understand the history and recent trends relating to excessive fee claims, the plan features that may make it a target of litigation, and steps fiduciaries can take that may reduce exposure to excessive fee claims.

## The Evolution of Excessive Fee Claims

Plan fiduciaries have a duty to ensure that plan recordkeeping and investment management fees are reasonable, and that plan investments perform well. In excessive fee claims, plan participants allege that plan fiduciaries failed on both counts and breached their fiduciary duties. Specifically, they allege that a plan is paying too much to its recordkeeper and investment manager. They also take aim at something called "revenue sharing," claiming that revenue sharing bloats the recordkeeping fees even more. Revenue sharing occurs when a mutual fund manager pays or "shares" part of its mutual fund's fees with the recordkeeper for purposes that are unrelated to the management of the mutual fund, such as a marketing fee. Finally, they allege that the plan is using investments that underperform their benchmarks.[1] Plan participants claim that these fiduciary breaches cost them millions of dollars in lost retirement benefits.

Excessive fee claims first emerged in 2006 and, for much of the last decade, these claims targeted very large 401(k) plans, meaning plans with tens of thousands of participants and billions of dollars in plan assets. That has changed in recent years with an increase in lawsuits against all types of plans (e.g., 403(b) plans, multiple employer plans, defined benefit pension plans, and even ERISA-exempt plans) and all types of plan sponsors (e.g., publicly traded companies, privately held companies, universities, not-for-profit organizations, financial institutions, and healthcare systems). Furthermore, the last few years have also seen an uptick in lawsuits involving smaller plans, including plans with fewer than 1,000 participants and less than $100 million in assets. Although it can be difficult to predict which plans will be targeted in the future, it is clear that fiduciaries of smaller plans should no longer consider themselves to be immune from this kind of litigation risk.

One of the reasons behind this increase may be that plaintiffs' law firms that were not previously known in the ERISA litigation space have started filing excessive fee claims. Using plan information obtained from public filings, these new entrants are able to easily model their complaints in "cookie cutter" fashion after those filed by more experienced firms that have honed their pleadings through years of experience in much bigger cases. In fact, the primary hurdle to bringing an excessive fee claim may be the ability of the plaintiffs' bar to recruit a plan participant to serve as a named plaintiff.

At the outset of a lawsuit, plan fiduciaries have the opportunity to move to dismiss a case by arguing that the facts alleged, even if true, do not constitute a breach of fiduciary duty. If the case is not dismissed at the outset, then it proceeds onto protracted discovery, which generally entails the review and production of thousands of documents as well as taking the testimony of numerous plan fiduciaries and other company employees. In addition, both sides retain costly expert witnesses. Some courts even allow for discovery to begin prior to the resolution of a motion to dismiss - giving plan participants the opportunity to uncover new facts to strengthen their allegations and making the case more expensive to defend from the outset. In this context, even a flawless legal defense of the best run plan can be an expensive and time-consuming endeavor, costing hundreds of thousands or even millions of dollars in defense costs.

These cases are not only expensive to defend, but they are also expensive to settle, with some of the largest settlements costing tens of millions of dollars.

## Predicting Which Plans Might Be Targeted

Due to the presence of new plaintiffs' firms in the mix and to constantly evolving theories of legal liability, it is difficult to predict which plans might attract unwanted attention. However, it appears that there are some plan characteristics that may make a plan more susceptible to being sued. Note that this is not meant to suggest that plans with such characteristics are paying excessive fees or engaging in imprudent or improper conduct. Rather, the following is a list of plan characteristics that have been targeted in the past, and thus may be targeted in the future:

- Accepting quoted recordkeeping rates without attempting to bargain up-front for lower fees, and/or failing to revalidate those fees via scheduled Requests for Proposals (RFPs) from recordkeepers.
- Paying recordkeeping fees as a percentage of assets under management rather than at a fixed per participant rate, and/or not switching to a fixed rate as plan assets grow.
- Failing to use the least expensive mutual fund share class available (e.g., institutional shares) as investment options.

1. Of course, these cases continue to evolve as plan participants test out new theories of liability, such as claims concerning the alleged misuse of plan participant data by recordkeepers.

- Failing to use separate accounts or collective investment trusts rather than mutual funds as investment options – but note that some complaints make the exact opposite allegation.
- Offering too few or too many investment options.
- Offering investment options that are too risky or too conservative.
- Failing to offer more index funds.
- Offering investment options, particularly life-cycle/target-date funds, that are affiliated with the plan's recordkeeper.
- Offering investment options that underperform net of expense relative to an index or benchmark.

Of course, plan fiduciaries may have good reasons to support the challenged decisions. And while those good reasons – and a thorough and well-documented process for making those decisions – can be critical to a successful defense of these suits, plan fiduciaries can expend significant time and money to prove that they acted with the appropriate level of care.

### Steps That May Reduce Exposure to Excessive Fee Claims

Under ERISA Section 409, fiduciaries are personally liable for a breach of fiduciary duty, including claims that they allowed the plan and its participants to pay excessive fees and use expensive and underperforming investments. Some fiduciaries mistakenly believe that they can entirely avoid this liability by hiring professionals to handle all of these decisions. Also, the law does not allow fiduciaries to totally delegate away all of their fiduciary responsibility.[2] So what can fiduciaries do to protect themselves? Of course, plan fiduciaries should always act with care and undivided loyalty to the plan and its participants. And while there is no foolproof way to avoid or defeat an excessive fee claim, there are some steps that may help to reduce the size of the bullseye on the backs of plan fiduciaries:

- Establish, follow, and document a robust and prudent process for retaining recordkeepers and determining their fees, including:
  - Periodically solicit RFPs through which a number of recordkeepers can submit competing bids for the plan's business
  - Benchmark recordkeeping fees using an appropriate, independent benchmark
  - Negotiate fees rather than accepting quoted fees without question
  - Investigate whether there is any revenue sharing being paid and consider negotiating limits on it
- Establish, follow, and document a robust and prudent process for selecting and regularly reviewing plan investments and investment expenses, including:
  - Select appropriate benchmarks for analyzing investment performance net of expense
  - Follow a consistent process for replacing underperforming investments
  - Investigate and consider the availability and advisability of using less expensive investment vehicles and share classes
  - Maintain a diverse portfolio of plan investment options, including index funds
- Retain qualified, independent experts to assist with fiduciary decisions – and don't rely on benchmarks provided by service providers who are justifying their own fees or performance
- Document the process and rationale behind any fiduciary decision, being meticulous when deciding to use more expensive products or services and/or when going against expert advice

As mentioned previously, plan fiduciaries can be held personally liable if they violated their fiduciary duties. Moreover, ERISA Section 410 bars plans from indemnifying plan fiduciaries against breach of fiduciary duty claims. Thus, a lynchpin of any loss mitigation effort is to obtain adequate fiduciary liability insurance. Breach of fiduciary duty claims under ERISA are precisely the type of exposure that fiduciary liability insurance is designed to protect against.

Some employees have employee benefits liability coverage as part of their general liability coverage; this provides coverage to an employer for errors or omissions in the administration of an employee benefit program. Employee benefits liability coverage will most likely not insure against an excessive fee claim, since these policies are designed to cover clerical administrative errors – not the fiduciary breach claims that take center stage in excessive fee litigation.

## Plan fiduciaries who do not have fiduciary liability insurance may be placing their personal assets at risk in the event of an excessive fee claim.

In light of this personal liability, plan fiduciaries who do not have fiduciary liability insurance may be placing their personal assets at risk in the event of an excessive fee claim.It's important to obtain fiduciary liability insurance from an experienced carrier that can successfully defend (and potentially settle) an excessive fee claim with as little disruption and stress as possible.

### Mitigating Corporate and Personal Risk

Even the most well-run plans can be the target of an excessive fee claim, which can cost millions of dollars to defend and/or settle. Fiduciaries of plans of all sizes should familiarize themselves with the basic allegations in these claims and review (and, if necessary, revise) how they select and monitor recordkeepers and plan investments. Last but not least, plan fiduciaries should obtain adequate fiduciary liability insurance from an experienced carrier to help mitigate and protect against potentially devastating, personal exposure to excessive fee claims.

2. Willett v. Blue Cross and Blue Shield of Alabama, 953 F.2d 1335, 1340 (11th Cir. 1992)

## About the Authors

**Alison L. Martin** is Senior Vice President and Fiduciary Product Manager for Chubb's North America Financial Lines division. Ms. Martin is responsible for the underwriting of all fiduciary liability products at the company, including coverages for publicly traded and privately held companies, not-for-profits, multi-employer plans and healthcare plans. She can be contacted via email at almartin@chubb.com.

**Lars C. Golumbic** is a Principal at Groom Law Group, Chartered, and Chair of Groom's litigation practice group. Mr. Golumbic is a nationally recognized ERISA litigator, and is listed by Chambers USA, The Legal 500, Best Lawyers, and Super Lawyers as one of the top ERISA litigators in the country. He can be contacted via email at lgolumbic@groom.com.

Chubb. Insured.℠

www.chubb.com/us/fiduciaryliability
The information contained in this document is intended for general informational purposes only and is not intended to provide legal or other expert advice. You should consult knowledgeable legal counsel or other knowledgeable experts as to any legal or technical questions you may have. Neither Chubb nor its employees or agents shall be liable for the use of any information or statements made or contained in any information provided herein. This document may contain links to third-party websites solely for informational purposes and as a convenience to readers, but not as an endorsement by Chubb of the entities referenced or the contents on such third-party websites. Chubb is not responsible for the content of linked third-party websites and does not make any representations regarding the content or accuracy of materials on such linked websites. The opinions and positions expressed in this report are the authors' own and not necessarily those of Chubb.
Chubb is the marketing name used to refer to subsidiaries of Chubb Limited providing insurance and related services. For a list of these subsidiaries, please visit www.chubb.com. Insurance is provided by ACE American Insurance Company and its U.S. based Chubb underwriting company affiliates. All products may not be available in all states. This communication contains product summaries only. Coverage is subject to the language of the policies as actually issued. Surplus lines insurance is sold only through licensed surplus lines producers. ©2020 Chubb. Form #17-01-0271 (Ed. 05/2020)