



Closing the Barn  
Doors after the Cows  
Have Left

## One Practitioner's View of Relevant ERISA Litigation

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# Agenda



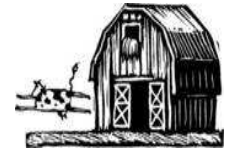
- The Barnyard
- ERISA Basics and Litigation Process
- Fiduciary Duties Litigation
- Fee Litigation
- Other Key Cases – Opinions and Settlements
- Investment Advice
- ERISA 408(b)(2) Notes
- The Future
- Implications for Practitioners

# Observations and Notes



- A non-attorney's view of ERISA litigation
  - Do not play one on TV, did not stay at a Holiday Inn Express...
  - Observations not necessarily one that an attorney would have
- Litigation and results are not just an attorney issue – affects *all* of us in this space
- The need to understand ERISA
- The need to understand case law
  - Each case is unique
  - Interprets ERISA
  - Case law continues to evolve
  - Settlements are worth examining

# The Barnyard



- ERISA plans are big economic targets
- Over \$18 trillion invested in US retirement plan assets
- \$4-5 trillion is invested in 401(k) and other “defined contribution” plans sponsored by private sector employers
- Over \$400 billion in defined contribution plans is invested in company stock
- New regulations
- Higher IRS and DOL visibility 1-800-yourbusted!
- Increasing sophistication of the plaintiffs’ bar
- Recession, market volatility and benefit cutbacks = POFEs

# ERISA Basics



- ERISA 404 (1) ...a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and--
  - (A) for the exclusive purpose of: (i) providing benefits to participants and their beneficiaries; and (ii) defraying reasonable expenses of administering the plan;
  - (B) with the care, skill, prudence, and diligence under the circumstances then prevailing [[Page 439]] that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;

# ERISA Basics



- ERISA 404 (1) ...a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and--
  - (C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and
  - (D) in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of this subchapter and subchapter III of this chapter.

# ERISA Basics



- Defines fiduciary ERISA 3(21)
- Defines party-in-interest ERISA 3(14)
  - And that includes anyone/everyone who touches the Plan
  - Define broadly – change behavior and practices
  - Define narrowly – be careful...
- “Know or should have known...”

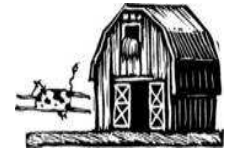
# ERISA Basics



- *Donovan v. Bierwirth*
  - Fiduciary Duties... “are highest known to the law”
  - Discharge duties with “the care, skill, prudence and diligence under the circumstances...”
  - Duty to engage experts in areas they do not know
- The Obligation:
  - *Ches v. Archer*
    - Delay in predecessor company making contributions
    - Successor company has the obligation to examine/pursue litigation against the predecessor company
  - ERISA 404(a)(1)
    - Trustee must discharge duties “solely in the interests...”



# Litigation Focus



- Litigation centered around
  - Who the fiduciaries are
  - The assertion that fiduciary duties were breached
  - The prudent selection of investments
    - Balance between prudence, eligibility and fees
  - That fees are too high
  - That fees and compensation to providers not disclosed sufficiently

# Litigation Process



- Mostly in federal court
  - Some governmental plans in state court
- Flow: Federal District Court → Court of Appeals → Supreme Court
- Cases tried – bench trial – no juries
- Damages – make whole – no punitive damages - “equitable relief” ERISA 502(a)(3)
- Opinions
  - Having the effect of interpreting ERISA as presented in the case
  - First in the home circuit and then across other circuits
- Circuits are not often consistent with each other

# Litigation Process



- Settlements
  - Not law but...
  - Not an admission of liability or “guilt” but...
  - Settle for a dollar amount and remedial actions proscribed
  - Practitioners: take note of reasons and why settled

# Fiduciary Duties Litigation



- At issue: Who are the fiduciaries?
  - Your plan sponsor client?
  - You?
- At issue: Are they acting in the best interests of the Plan participants?
- *Ellis v. Rycenga Homes*
  - Broker acted as a fiduciary advising plan administrator regarding plan assets
- *Variety v. Howe*
  - Fiduciaries must not mislead participants
- *CIGNA Corp. V. Amara*
  - Make sure SPDs are correct
  - Door opened for “surcharges” beyond equitable relief

# Fiduciary Duties Litigation



- *Tittle v. Enron*
  - Directed trustee has some liability – know or should have known....
  - Know of fraud or evil doings – must disclose and remedy
  - Head in the sand does not work
- *George v Kraft Foods*
  - Recordkeeping fees were 2x of plans of similar size
  - Imprudent not to get provider quotes periodically (RFP)
  - Could have picked index funds as in the DB plan but did not for the DC plan – rationale for active choices not clear
  - Co. fids did not follow consultant's advice and counsel

# Fiduciary Duties Litigation



- *LaRue v. DeWolff*
  - Participant's transfer instructions not executed timely
  - Plan Sponsor liable for difference
  - Be aware of duties/liability if you have discretionary control of a participant's account
- *Pfeil v State Street Bank*
  - ERISA 404 (c) protection does not extend to the overall fiduciary duty of selection and monitoring of investments
  - Having a poor investment in an otherwise good line-up is akin to "one bad apple" spoiling the whole bunch
  - Participant are not the fiduciaries when they put their contributions/balances into a poor performing fund - goes beyond §404(c) protection.
  - The duty of a fiduciary to monitor *all* investments reaffirmed

# Fiduciary Duties Litigation



- *Skinner v. Northrop Grumman*
  - Brings trust law (adopted by the states) into the process
  - *A trustee (or a fiduciary) who gains a benefit by breaching his or her duty must return that benefit to the beneficiary* Third restatement of the Laws of Trust
  - *A trustee who breaches his or her duty could be liable for loss of value to the trust or for any profits that the trust would have accrued in the absence of the breach.* Third Restatement of the Laws of Trust and Third Restatement of Trust – Restitution and Unjust Enrichment
- While the plaintiffs did not get what they wanted:
  - State trust law is now on the record
  - Issue of recoupment is on the record
  - Issue of surcharges (damages) in ERISA cases is again on the record
  - Implications for 403(b) and non-ERISA plans

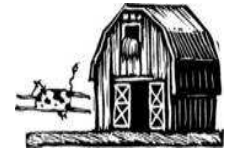
# Fiduciary Duties Litigation



- *Tussey v. ABB*
  - Company did not follow IPS – rebates and rebate monitoring required but not performed
  - Added a more expensive fund replacing a significantly less expensive fund.
  - Company had minimal oversight over payments, costs and fees to service provider
  - Meaningful fund fee benchmarking not performed
  - Company did not track float income
  - Provider (a fiduciary) breached its duties in not distributing float income
  - When distributed – to the wrong places
  - Fiduciaries held liable for \$21.8 mm and an additional \$1.7 to be added to the plan



# Fiduciary Duties Litigation



- *U.S. v. Benjamin Eichholz* criminal and civil case
  - Sole fiduciary of two plans
  - Ran plan like a personal fund (funds were missing)
  - Did not file IRS 5500s
  - Many, many PTs including lying to DOL examiners
  - Plan provisions violated (issue loans)
  - Personal items (fine china) were plan assets
  - Defendant serving a 21 month sentence
  - Civil charges pending

# Fee Litigation



- At issue: Are fees excessive?
  - Retail v institutional shares
- At issue: Does plan administrator know them? (are we disclosing to the PAs?)
- *Hecker v. Deere, Loomis v. Exelon, Renfro* and other related cases
  - Retail shares OK if large range of investments offered and sufficient number are passive/index/ low cost.
  - Funds in Hecker (>60), Loomis (>30), Unisys (>70)
  - Cheap is not necessarily best
  - Show a consistent process for selection/monitoring

# Fee Litigation



- *Tibble v. Edison*
  - Three retail funds were in plan with nearly identical funds in cheaper share classes available
  - Plan was eligible for cheaper share classes
  - Issues with investment selection
  - Retail shares (fees) were not appropriate here

# Fee Litigation



- Settlement: *Braden v. Wal-Mart*
  - American Funds Class A shares for this multibillion dollar plan
  - Limited investment selection
  - Settlement amount: \$13.5 mm
    - Provider to provide \$10mm
    - Wal-Mart to provide \$3.5 mm
  - Remove Class A shares and add index funds
  - Comply with fee disclosure regulations

# Other Key Cases



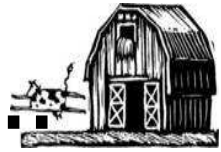
- Settlement: *Phones Plus v. Hartford*
  - Hartford acted as a fiduciary in fund selection
  - Hartford designed investment menus based on compensation
  - Hartford failed to disclose fees received
  - Settlement \$13.8mm
- Settlement: *Martin v. Caterpillar*
  - Internal investment staff ran investment funds
  - Failure to monitor plan investments
  - Fee issues and internal conflict of interest issues
  - Settlement \$16.5 mm

# Other Key Cases



- Procedural process
  - Seen a lot in stock put-back ESOP cases
- *DelRosaro v. King & Prince Seafood Corp.*
  - Issue of discretionary duties in a plan
  - Payment consistency: changed payment criteria each year
  - Payment inconsistency benefitted Co. officers
  - **Don't make up policies and valuation steps as you go along**

# Closing the Barn Door Before..



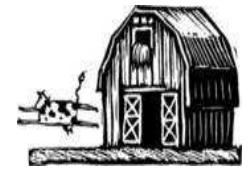
- Recognize exposure at least as a party-in-interest – you have some
- Be clear on fiduciary role taken and disclose appropriately – act accordingly
- Be careful about providing investment advice at plan or participant level and are not “a fiduciary” You are!
- Your IPS? Enforce it and make sure clients understand what they have.
- Add retail funds carefully – especially when institutional funds are available and are eligible

# Closing the Barn Door Before...



- Take stand against client governance compromises or shortcuts
- Advise client of errors/wrong practices *even if you are not engaged in that area*
  - “...know or should have known...”
- Disclose/exceed requirements in the spirit of disclosure
- Think twice about having 70 funds in a plan and thinking that is a good selection
  - Still need to perform due diligence on plan’s funds
  - What confronts participants with 70 funds?
  - How does a participant choose between four + large cap blend funds? Three intermediate bond funds, etc.? Why?





Questions?