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Addressing Excessive Fee Litigation Risk in the Wake of Hughes v. Northwestern

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The Supreme Court's January 24, 2022 decision in *Hughes v. Northwestern University*, has caused alarm in some corners, with panicked predictions of a proliferation of ERISA suits alleging that defined contribution plans provided imprudent investment options. However, *Hughes* should be more properly understood as rejecting an attempt by the U.S. Court of Appeals for the Seventh Circuit to impose a novel limit on excessive fee suits. The Supreme Court instead emphasized the application of its existing precedent in *Tibble v. Edison International,* 575 U.S. 523 (2015).

The Seventh Circuit had dismissed a class action complaint alleging the trustees of Northwestern Universities' retirement plans breached their fiduciary duties by including imprudent investments among the investment options offered under the plans. The trustees offered more than 400 various investment options, several of which the plaintiffs asserted were imprudent and many of which were not. The Seventh Circuit held that the plaintiffs' allegations failed as a matter of law (that is, could be dismissed without discovery or trial) because plaintiff's preferred investment options were available under the plan (albeit alongside the allegedly imprudent options). Therefore, the Seventh Circuit considered the trustees to be blameless for any fiduciary breaches because the plaintiffs simply could have avoided the allegedly imprudent investments and chosen the prudent ones.

Justice Sotomayor's unanimous opinion in *Hughes* rejected this logic, holding that the presence of prudent investment options among the choices available to participants in defined contribution plans cannot, by itself, excuse the inclusion of imprudent investment options. This holding comports with the Supreme Court's 2015 *Tibble* decision that held "a plaintiff may allege that a fiduciary breached the duty of prudence by failing to properly monitor investments and remove imprudent ones."

Hughes serves to remind fiduciaries of defined contribution plans that they should regularly assess investment options for suitability, purge imprudent options, and retain only those that remain suitable. Simply adding additional, prudent options will not avoid liability for retaining bad ones.

Therefore, fiduciaries should be on the lookout for "red flags" that plan investment options may no longer be suitable. Investments often charge different management and record keeping fees depending on the size of the plan. Fiduciaries should recognize that, as plans grow, lower fee versions of existing offerings may become available; the opportunity to lower costs to participants should be seized as soon as it arises. Fiduciaries who fail to make the switch risk incurring liability.

As a best practice, fiduciaries should retain investment consultants to research the availability of lower-fee versions of existing investment options. The subjects of ongoing excessive fee litigation provide another “red flag.” Flaws which render a particular product unsuitable for one plan, often render the product unsuitable for other plans. (The use of a product identified as flawed in a lawsuit involving another plan will, in any event, attract the attention of plaintiffs’ lawyers, which will underscore the need to review its inclusion in a different plan.) Fiduciaries should consult with their counsel to obtain updates regarding funds that have become litigation targets and more closely scrutinize them or offerings that may exhibit the same flaws. Responding to these “red flags” will go a long way towards limiting litigation risk.

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