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Top US Universities Hit with Retirement Plan Lawsuits: Lessons for Plan Sponsors

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Summary

The recent wave of 403(b) lawsuits against more than a dozen prominent US universities could herald similar suits for other 403(b) plan sponsors. Plan sponsors can minimize their risk by reviewing their plan governance procedures, investment policy statements, and plan investment lineup and fee structure.

In Depth

Sponsors of 403(b) plans should pay close attention to retirement plan investments and fees. More than a dozen class action lawsuits have been filed against a number of large US universities, arguing that the universities selected investments for their retirement plans that charged the plan participants excessive fees in violation of fiduciary duties under the Employee Retirement Income Security Act of 1974 (ERISA). The plaintiffs' bar has succeeded in obtaining substantial settlements in a number of similar cases against 401(k) plans, but these suits are new in the world of 403(b) plans. If the plaintiffs succeed in obtaining similar outcomes, other 403(b) plan sponsors will likely end up fighting similar suits. To minimize the risk of litigation and strengthen their position to defend such lawsuits, 403(b) plan sponsors should review their plan governance procedures, investment policy statements, and plan investment lineup and fee structure.

ERISA imposes strict duties on fiduciaries to act solely in the interest of, and for the exclusive purpose of providing benefits to, plan participants and beneficiaries. ERISA permits plan participants to file suit against plan sponsors for alleged fiduciary breaches. Fiduciaries can be held personally liable for losses resulting from such breaches, and the potential stakes involved are high. In one pending case, the plaintiffs have asked the court to hold the defendants personally liable for an alleged $100 million in losses of the retirement plans.

The complaints that have been filed so far generally assert the same types of claims:

- That the plan fiduciaries breached their duties of loyalty and prudence under ERISA by charging participants unreasonably high administrative fees. As is common in the 403(b) space, the plans at issue use multiple recordkeepers. The suits allege that the defendants

should have instead consolidated their plans' administrative and recordkeeping services under a single service provider at a lower cost. The suits also allege that the defendants failed to solicit competitive bids from other recordkeepers and allowed the plans' recordkeepers to receive asset-based revenue sharing. The plaintiffs claim that the defendants failed to monitor these payments and that the fees were not reasonable in light of the services provided.

- That the plan fiduciaries breached their duties of loyalty and prudence under ERISA by paying unreasonably high investment management fees and by exposing the plans to performance losses. The plaintiffs allege that the defendants selected investment options with higher expenses and poorer performance relative to other available investment options, and that the defendants also confused plan participants by offering a large number of investment options. The plans' investment options allegedly included retail share class mutual funds as opposed to institutional share class funds, which have lower fees and are designed for large institutional investors such as retirement plans.

- That the universities, as monitoring fiduciaries, breached their duty by failing to monitor their appointees, to evaluate their performance (including with respect to the investment and holding of plan assets and the payment of administrative and revenue sharing fees), and to have an evaluation system in place (including for the removal of underperforming appointees).

- In one case, that the defendants caused the plan at issue to engage in a "prohibited transaction" under ERISA by allowing the plan's recordkeeper to both serve as recordkeeper *and* separately be paid through direct and indirect revenue sharing payments resulting from the plan's investments with the recordkeeper's company.

Next Steps

Plan sponsors and their investment committees and other fiduciaries can take concrete steps to minimize their risk of litigation.

- Plan sponsors should review their plan governance procedures and service agreements with recordkeepers to ensure that their recordkeeping and other administrative costs are either below or in line with market rates. It is advisable to engage an outside advisor to assist with the review of plan fees and expenses.

- Plan sponsors should review any investment policy statements to ensure that they have a proven process in place for selecting investments. If a retirement plan has no written investment policy statement, plan sponsors should consider putting one in place to make their decision-making process as transparent as possible.

- Investment committees should eliminate underperforming investment funds and prepare easy-to-understand participant communication materials about the different investment options that are available to reduce confusion.

- Investment committees should conduct regular requests for proposal (RFPs) and fee benchmarks to see if there is a lower-cost third-party service provider available.

- Investment committees should carefully document their decision-making process in writing.

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