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2024 Excessive Fee Litigation Webinar

The Current State of Fiduciary Excess Fee and
Imprudent Investment Litigation

by Daniel Aronowitz, President, Encore Fiduciary

January 30, 2024 | 12:00-12:30 EST

About our Speaker



Daniel Aronowitz, J.D. RPLU+
President
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Daniel Aronowitz is the President of Encore (formerly Euclid) Fiduciary, a leading Fiduciary Liability insurance underwriting company for America's employee benefit plans. He has over thirty years of experience in the professional liability industry as a coverage lawyer and underwriter and is a widely recognized fiduciary liability expert and thought leader. He is the author of The **Fiduciary Liability Insurance Handbook**, **The Fid Guru Blog** and the fiduciary liability insurance chapter of the **Trustee Handbook** published by the International Foundation of Employee Benefit Plans. He is a graduate of The Ohio State University and Vanderbilt University School of Law and has achieved the RPLU+ designation from the Professional Liability Underwriting Society.

Agenda



- **Excess Fee Cases Statistics:** The number of cases; plaintiff law firms; size of plans being sued.
- **Types of Excess Fee Cases:** (1) Excess Recordkeeping Fees; (2) Excess Investment Fees; and (3) Imprudent Investment Cases.
- **Court Rulings:** Key Appellate Decisions; and the Pleading Standard for Excess Fee Case – Motion to Dismiss Statistics.
- **Settlement Statistics for Excess Fee Cases**
- **Final Analysis**

What is an Excessive Fee Lawsuit?



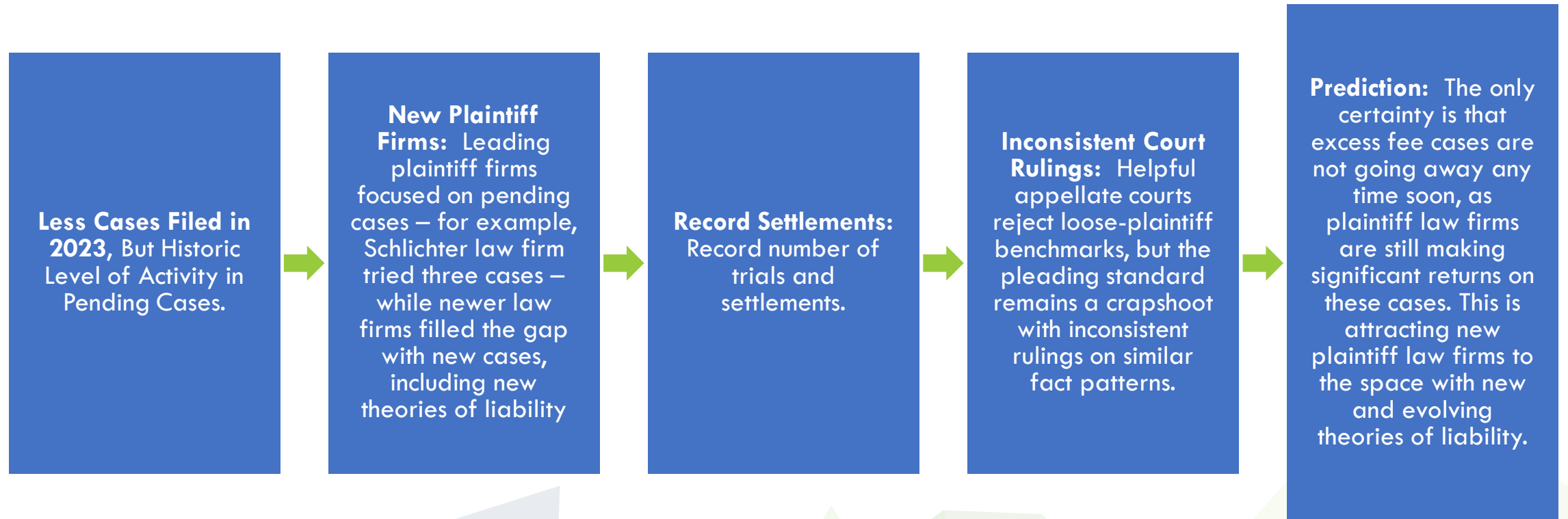
Three primary excess fee and imprudent investment claims:

- Plan recordkeeping fees are too high
- Plan investment fees are too high
- Plan investment performance is too low

The lawsuits seek damages in the amount of purported excessive recordkeeping and investment fees, and purported amount of investment underperformance.

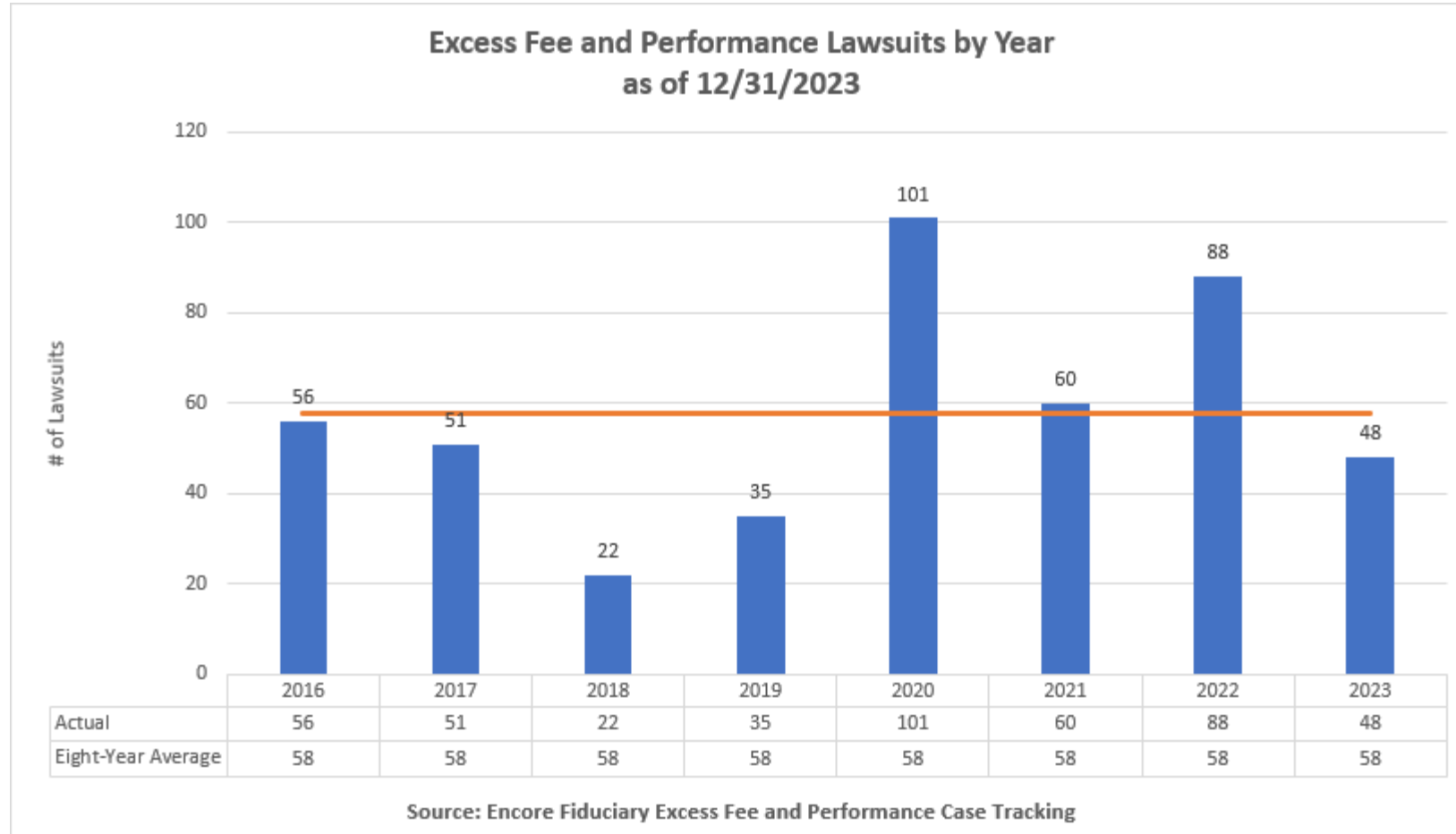
The State of Excess Fee Litigation

Excess Fee Litigation Remains at a Fever Pitch



Frequency

48 Cases Files in 2023 – A Decrease from 2022 as Legacy Firms Digested Substantial Case Backlog



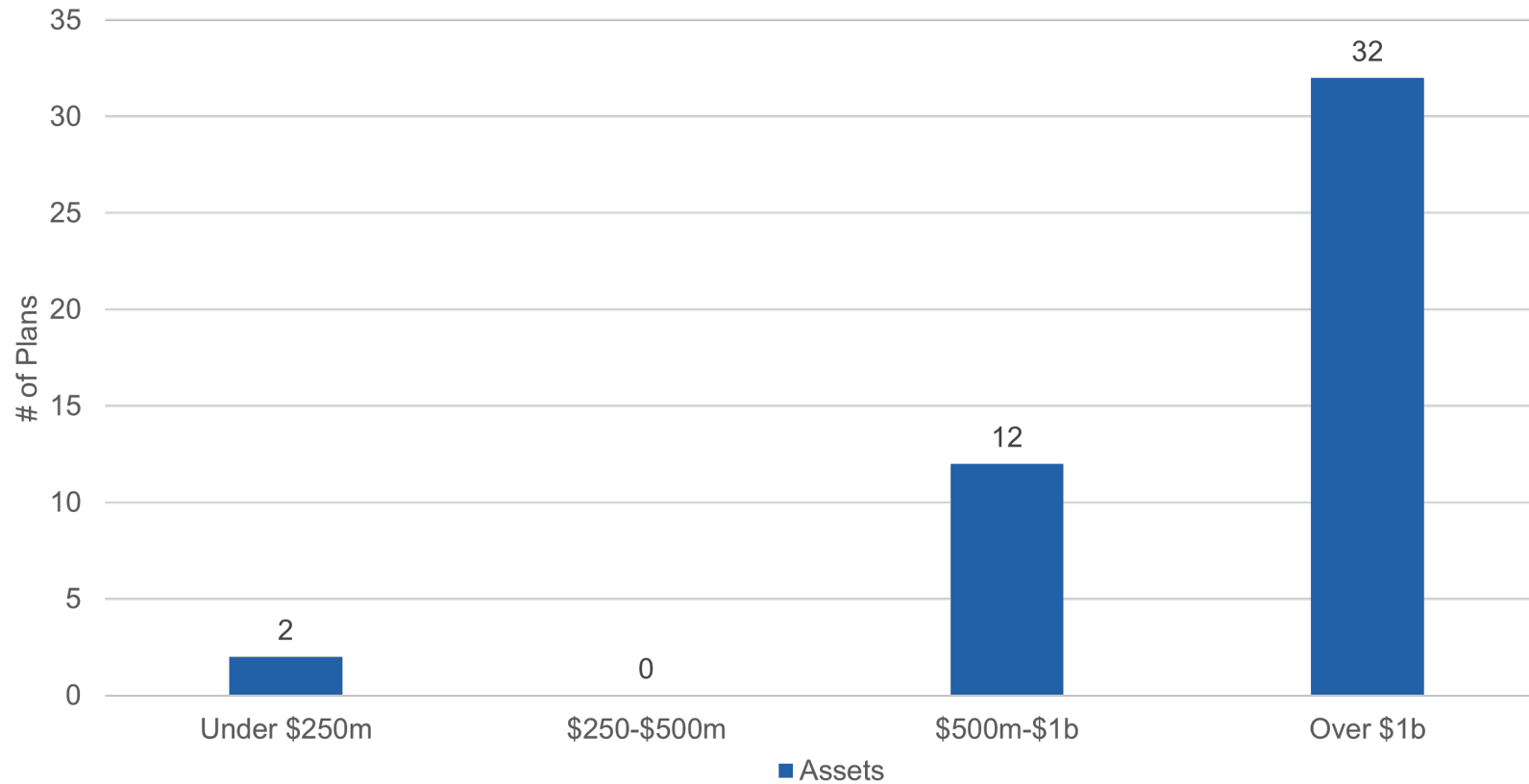
New Plaintiff Law Firms Leading the Charge in 2023



2022 Filings		2023 Filings	
PLAINTIFF LAW FIRM	2022 # OF CASES FILED	PLAINTIFF LAW FIRM	2023 # OF CASES FILED [INCLUDING WHEN FILED JOINTLY WITH ANOTHER LAW FIRM]
Capozzi Adler	21	Wenzel Fenton Cabassa	10
Miller Shah	15	Christina Humphrey Law	4
Walcheske & Luzi LLC	13	Walcheske & Luzi	8
Wenzel Fenton Cabassa	11	Morgan & Morgan [in conjunction with Wenzel Fenton Cabassa]	7
Nichols Kaster	8	Nichols Kaster	2
Tower Legal	4	Tower Legal Group	2
Schlichter Bogard & Denton, LLP	3	Capozzi Adler	6
Fair Work	2	Hayes Pawlenko	5
Baillon Thome Jozwiak & Wanta LLP	2	Bailey & Glasser	2
Roberts Law	1	Cohen Milstein	1
Sanford Heisler Sharp, LLP	1	Sanford Heisler	1
Other firms	7	Izard Kindall & Raabe	1
		Foulston Siefkin	2
		Edelson Lechtzin	1
		McKay Law	1
		Ducello Levitt [but note the complaint follows the Walcheske template]	1
		Hacker Stephens	1
		Sharp Law LLP	1
		Pomerantz LLP	1
		Scott & Scott	1

The Year of Lawsuits against Jumbo Plans

2023 Excess Fee Lawsuits – By Size of Plan



2023 Types of Excess Fee and Investment Imprudence Claims

2023 Filings	
Excessive Recordkeeping Fees	28
Excessive Investment Fees	17
Deficient Investment Performance – Investment Imprudence	23
Wrong Share Class	11
High Fee / Underperformance of Active TDFs	10
Excess Float Income	9
Proprietary Funds	7
Forfeiture Claims	5
Stable Value Fund Claims	4
Excessive Managed Account Fees	1
Other (self-dealing)	1

Excess Recordkeeping Fee Claims – What is Being Alleged?



- **The Fees Being Alleged as Excessive Are Often False: Complaints use Form 5500 fees that are inflated with transaction fees unrelated to recordkeeping:**
 - EXAMPLE: *Teodosio v. Davita, Inc.* (D. Colo. 07/08/2022): court accepted as “true” for purposes of a motion to dismiss that the plan paid between \$50-96 for recordkeeping services worth between \$14-21. But here are the true facts not alleged in the complaint:
 - Named plaintiffs with tiny account of less than \$750 paid between 12 cents and \$10.56 for recordkeeping services – nowhere close to the alleged plan fees.
 - But the fees alleged were false: In motion to dismiss, the defense provided evidence from the plan’s recordkeeping contract and fee disclosures that the plan’s recordkeeping fee was \$37 per participant, until 2020 when the fee was reduced to \$34.50; The recordkeeping fee was paid for through a combination of revenue sharing from certain plan investment options and direct participant charges, with Voya refunding any “excess” revenue sharing it received to the plan above the maximum fee [in other words, the fee to Voya was capped at \$37.00, and then \$34.50 – not the \$50-96 alleged in the complaint];
 - But the strategy worked: Case settled for \$2 million.
 - EXAMPLE: *Dukes v. Amerisource Bergen Corporation* (W.D. Ky. 07/19/2023) [\$700.4m/4656]: Plaintiff-participant received a fee disclosure with a \$48 RK fee from 2017-2021, which was reduced to \$36 in 2022. But the complaint alleged from Form 5500 that the recordkeeping fee was \$61 per participant – a purported 96% premium from the \$30 benchmark.

Types of Recordkeeping Benchmarks Used in Excess Fee Cases



- **Plaintiff Benchmark #1: Distorting the small-plan recordkeeping statistics from the 401k Averages Book.**
 - Claiming that \$200m plans only pay \$5 per participant – intentionally leaving out the survey results that the same plan pays \$160 per participant in revenue sharing.
- **Plaintiff Benchmark #2: Allege that Fidelity has stipulated that its recordkeeping services are only worth \$14-21 per participant.**
 - EXAMPLE: *Winkleman v. Whole Foods Market, Inc.* (W.D. Tex. 11/06/2023): Plaintiffs allege \$31 recordkeeping fee is imprudent compared to \$14 contrived benchmark from Fidelity discovery stipulation in the *Moitoso* case involving Fidelity's internal 401k plan.
- **Plaintiff Benchmark #3: Chart of Random Large Plans with Purportedly Low Recordkeeping Fees.**
 - The chart in *Ulch v. Southeastern Grocers* (M.D. Fla. 09/27/2023) alleges that the \$1.4B/10,070 Netflix 401(k) Plan only pays \$4.17 per participant; and the \$1.3b/10,039 RPM International Inc. 401(k) Plan only pays \$9.23 per participants.

Key Issues in Excess Recordkeeping Claims



- **(1) Key determinant is whether the court will allow evidence outside the MTD, including fee disclosures and account statements that include the actual fees.**
 - False Recordkeeping and Investment Fee Claims – Can the Defense Use Fee Disclosures and Account Statements to Rebut False Fee Claims?:
 - EXAMPLE: *Matousek v. Mid-Am. Energy Co.*, 51 F.4th 274 (8th Cir. 2022): Complaint alleged that the plan recordkeeper for the MidAmerican Energy plan charged an “unreasonable” fee ranging “between \$326 and \$526 per plan participant,” but the truth was that the actual recordkeeping fee was only \$32 per participant.
- **(2) What are Proper Benchmarks?**
 - Plaintiffs are taking advantage of the lack of a comprehensive benchmark for what large plans actually pay for recordkeeping services. **But see** the Encore Fiduciary Benchmark.
- **(3) Is Recordkeeping for large plans commoditized, or are there differentiation in services?**
 - In 2023, complaints started citing Form 5500 service codes: *Cina v. CEMEX, Inc.* (S.D. Tex (02/21/2023) – complaint against a \$877.8m plan alleges a \$74 recordkeeping fee from the plan fee disclosure, which is compared to four comparator plans with the same Form 5500 service codes [37, 60, 64, 65, 71].
 - *Carrillo v. Amy’s Kitchen* (N.D. Cal. 06/16/2023): complaint alleges that plaintiff attorneys sent the Form 5500 of the Amy’s Kitchen plan and received lower bids of \$44 and \$60 per year.

New Theories of Liability



○ Failure to Monitor Float Income:

- Imprudence claim that plan fiduciaries failed to monitor float interest in the clearing accounts of the plan's recordkeeper.
- Original float claims brought in 2016 against Fidelity, but this is the first time that float claims have been brought against plan sponsors.
- Example: *Barner v. McLane Company, Inc.*, No. 6:23-00301 (W.D. Tex filed 04/24/2023), the complaint alleges that Merrill Lynch was permitted under its recordkeeping contract to allow participant deposits or money withdrawn from the plan from individual accounts to first pass through a Merrill Lynch clearing account. McLane allegedly agreed that any investment returns and/or interest earn on plan participant money in the clearing account – typically 2-3 days – belongs to Merrill Lynch. The complaint asserts that this additional compensation of even a 1% return on \$263,000,000 would account for \$2,630,000 in indirect float compensation. Plaintiffs allege that McLane imprudently permitted Merrill Lynch “to siphon millions of dollars from the Plan.”

○ Plan Forfeitures

- A California law firm has filed five cases to date challenging the widespread practice of using plan forfeitures – the nonvested portion of a former employee's account balance – to offset employer contributions.
- The lawsuits allege that using plan assets to offset employer contributions is self-dealing that violates ERISA's prohibited transaction rules and ERISA's fiduciary requirement that plan assets be “for the exclusive purpose” of paying benefits or plan expenses.
- In all five cases, plan documents allowed the plan sponsor to offset employer contribution. Question is whether plan document that allow any discretion or choice as to whether to offset contribution turns this into a fiduciary function that must be made in the sole interest of participants.

Excess Investment Fee Claims



Many Cases Involve Misleading Fees, Including Revenue Sharing is Rebated

- **Active to Passive** - Most investment fee claims compare active investments to index funds with lower fees.
- **Share Class Claims** – the most difficult to dismiss.
- **Investment Fee Claims Involving Revenue Sharing:**
 - ***Matney v. Barrick Gold of North America:*** Plaintiffs alleged that the JP Morgan Smart Retirement R5 target-date funds ranged in fees from .55-.57%, whereas the R6 share class had a lower .44-.47% fee. The difference between the R5 and R6 share classes was ten basis points in most instances. Utah District Court granted the motion to dismiss because plaintiffs ignored the 15-basis point revenue sharing credit back to participants. The District Court of Utah in the *Barrick Gold* case [which was affirmed on appeal] allowed the defense to proffer evidence of the recordkeeping contract and the participant account statements to demonstrate that the plan paid less than the institutional share-class fees because of a significant 15 bps revenue sharing rebate back to plan participants.
 - **KEY POINT:** court allowed the defense to produce the Trust Agreement and 2018 Form 5500 to validate that the plan implemented a revenue credit that was not alleged properly in the amended complaint.
 - ***Shave v. CentraCare Health System*** involved: (1) the exact same JP Morgan target-date investments; (2) the exact same fees charged by JP Morgan; (3) the exact same revenue sharing rebates that reduced the fees paid by participants below the lowest-fee institutional share class price; and (4) the respective plaintiff law firms in both cases misrepresented the actual investment fees paid by participants.
 - But the District of Minnesota Court refused to consider the plan participant account statements, fee disclosures, or recordkeeping contract in the context of a motion to dismiss. This evidence proved the identical 15 bps rebate that the *Barrick Gold* court used to dismiss the complaint, but the Minnesota court ruled that it must allow the claim to proceed even if it is “improbable.”

Imprudent Investment Fee Claims



More Imprudent Investment Claims & First ESG Lawsuit Against a Single-Employer Plan

- *Macias v. Sisters of Leavenworth Health System*, filed 06-13-2023 (D. Colo.) – alleging “mediocre” and “chronic underperformance” of the JP Morgan Smart Retirement target-date funds.
- *Fitzpatrick v. Nebraska Methodist Health System, Inc.*, filed 01-24-2023 (D. Nebr.) – alleging “chronically underperforming Wells Fargo target date funds.
- *Drust v. Southwest Research Institute*, No. 5:23-cv-00767-XR (filed 06/16/2023 W.D. Tex.): complaint alleges underperformance of TIAA funds, asserting that the plan sponsored \$1.5B plan sponsored by Southwest Research Institute is the only ERISA plan in the country with over \$250 million in assets (out of 9,000) to have an exclusive TIAA investment lineup.
- *Baker v. The University of Vermont Medical Center, Inc.*, No. 2:23-cv-87 (D. Vt. Filed 05/10/2023): complaint alleges imprudence for retaining ten TIAA-CREF legacy investment options.
- **First ESG Lawsuit:** Lawsuit alleges American Airlines selected and included twenty-five or more investment options in its sponsored defined contribution plan that are more expensive and underperformed, or otherwise included funds from investment managers who voted for egregious examples of ESG proxy mandates. After AA proved in the motion to dismiss that it has zero ESG investment options, the case has morphed into conflicting theories that AA’s fiduciary committee should have pressured Blackrock’s proxy voting to avoid woke-ESG mandates.

Three Key Issues in Imprudent Investment Fee Claims



1) What is the performance benchmark for investment underperformance?

- Does the comparison need to be against an investment with similar aims, goals and objectives; or can you compare to the S&P 500 or some other index?

2) What is the level of investment performance sufficient to be imprudent – is 1-2% underperformance enough?

3) How long before fiduciaries have to replace an underperforming investment?

- Plaintiff experts are testifying in many cases that investments must be dumped after less than 36 months of underperformance or even one year on the watchlist.
- ***Jacobs v. Verizon Communications, Inc. (April 20, 2023)***: New York court relied on plaintiff's expert testimony that it is imprudent for fiduciaries to retain an investment that underperforms for twelve consecutive quarters. After summary judgment denied, Verizon settled for \$30 million.

Motion to Dismiss Rulings

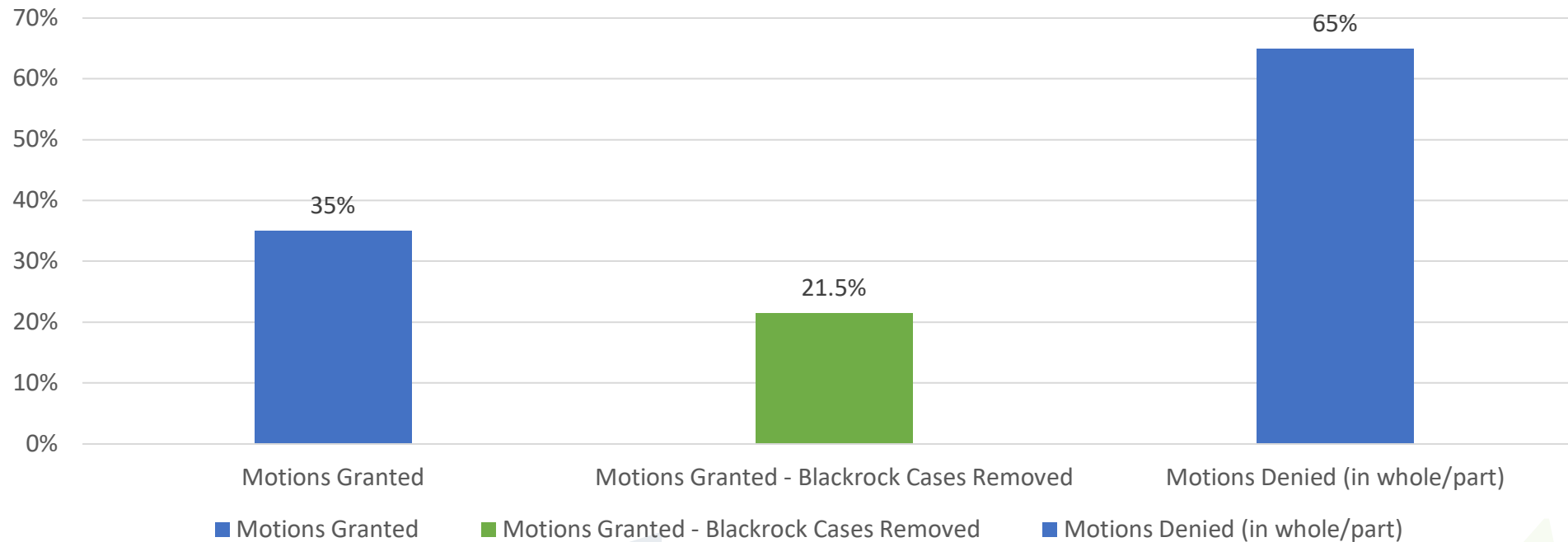


- Evolving theory that plan sponsors are winning more cases after favorable appellate decisions, but the reality is that over two-thirds of cases withstand a motion to dismiss:
 - The number of cases surviving a motion to dismiss is largely unchanged
 - Even cases in favorable jurisdictions like the Sixth and Seventh Circuit survive the pleadings stage
- **THE NUMBERS:** 70 motions to dismiss filed in 2023 – a record number of rulings in one calendar year.
 - Most Cases Continue to Survive the Pleading Stage:
 - Only 24 motions granted [35%].
 - But the success rate is only 21.5% if the quixotic Blackrock cases taken out [nine dismissals in 2023].
- **Case results are still a frustrating crapshoot:**
 - Compare two Fidelity Freedom case results:
 - *Smith v. CommonSpirit* – dismissed by the Sixth Circuit
 - *In re Biogen, Inc. ERISA Litig.* (D. Mass. 08/24/2023) – settled for \$9.75m with the same exact investment at issue in the *CommonSpirit* case.

Motion to Dismiss Rulings

Motions to Dismiss are granted 35% of the time – but only 21.5% if Blackrock Cases Removed

2023 Motions Granted v Motions Denied



Note: Motions denied in part are counted as a denial

Key Appellate Court Rulings – the Pleading Standard for Excess Fee Claims



- **Supreme Court:** *Hughes v. Northwestern University*: Courts “must give due regard to the range of reasonable judgments a fiduciary may make.”
- **6th Circuit:** *Smith v. CommonSpirit; Forman v. TriHealth*.
- **7th Circuit:** *Albert v. Oshkosh* and *Hughes v. Northwestern* – Part 2 [after Supreme Court remand].
- **Eighth Circuit:** *Matousek v. MidAmerican Energy Co.* – affirmed dismissal of recordkeeping and investment fee/performance claims.
- **9th Circuit:** In a pair of unpublished decisions, reversed dismissal of recordkeeping, share-class claims and CIT v mutual-fund claims (but rejected plaintiffs’ comparisons of active v. passive funds). *Kong v. Trader Joe’s* and *Davis v. Salesforce.com*.
- **10th Circuit:** *Matney v. Barrick Gold* – Affirmed dismissal of share-class claims, investment management fee claims, CIT v. mutual fund claims, and recordkeeping claims.

Prohibited Transaction Claims



Split of Authority in the Ninth and Second Circuits

- **Ninth Circuit:** In *Bugielski v. AT&T Services, Inc.*, in August 2023, the U.S. Court of Appeals for the Ninth Circuit held that amending an existing recordkeeping contract constituted a prohibited transaction because the recordkeeper was already a party in interest, disagreeing with the U.S. Court of Appeals for the Third Circuit that it “would be absurd” “to prohibit necessary services” unless there was “an element of intent to benefit a party in interest.”
- **2nd Circuit:** *Cunningham v. Cornell University* in November 2023, the U.S. Court of Appeals for the Second Circuit held that a plaintiff cannot survive a motion to dismiss merely by alleging that a presumptively prohibited transaction took place. Instead, the Second Circuit held that a plaintiff must plausibly allege both that a prohibited transaction occurred, and that no exemption applies, disagreeing “with the Eighth Circuit that, at the pleading stage, the . . . Exemptions should be understood merely as affirmative defenses.”

Lessons From Five Excess Fee Trials in 2023



○ **Record Number of Trials in 2023:**

- Yale
- E.B. Braun
- Wood Group – decision pending in C.D. Calif.
- Molina Healthcare – decision pending in C.D. Calif.

○ **Investment and recordkeeping fee changes are proof positive of proper fiduciary management. The most effective way to prove fiduciary best practice is a record of changes:**

- Yale consolidated to one recordkeeper before the lawsuit.
- E. B. Braun: trial evidence that committee removed underperforming funds and transitioned to the CIT and lower-fee share classes.

Key Pending Cases in Federal Appellate Courts



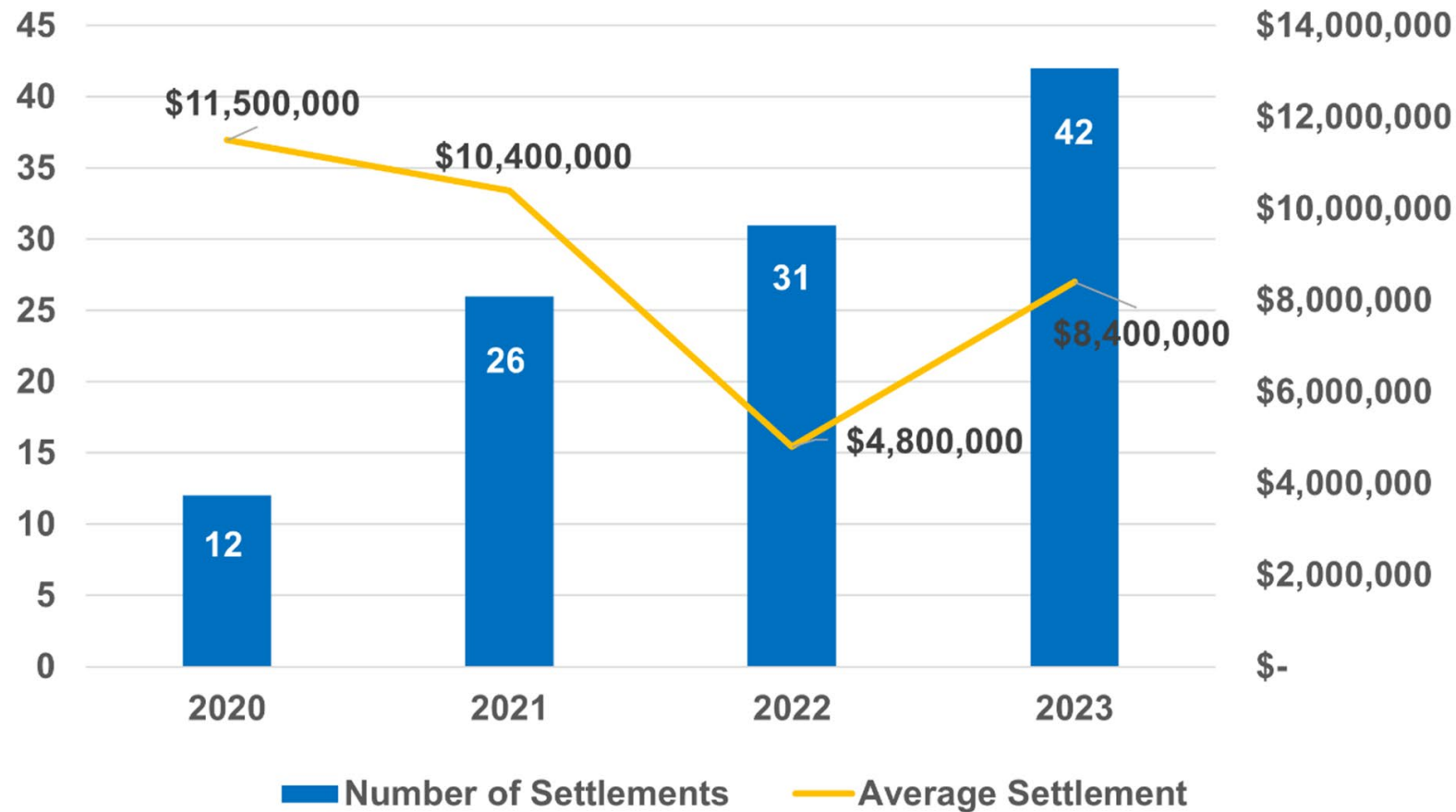
- Home Depot appeal – key issue of loss causation
- Goldman Sachs appeal- proprietary investment case.
- Wesco Appeal – appeal pending in *Mator v. Wesco* (W.D. Pa.) [argued April 18, 2023], which dismissed recordkeeping and share-class claims.
- Yale trial appeal – what is the burden of proof for loss causation?
 - “could have” or “should have” a prudent fiduciary made the same decision

A Record Number of Settlements

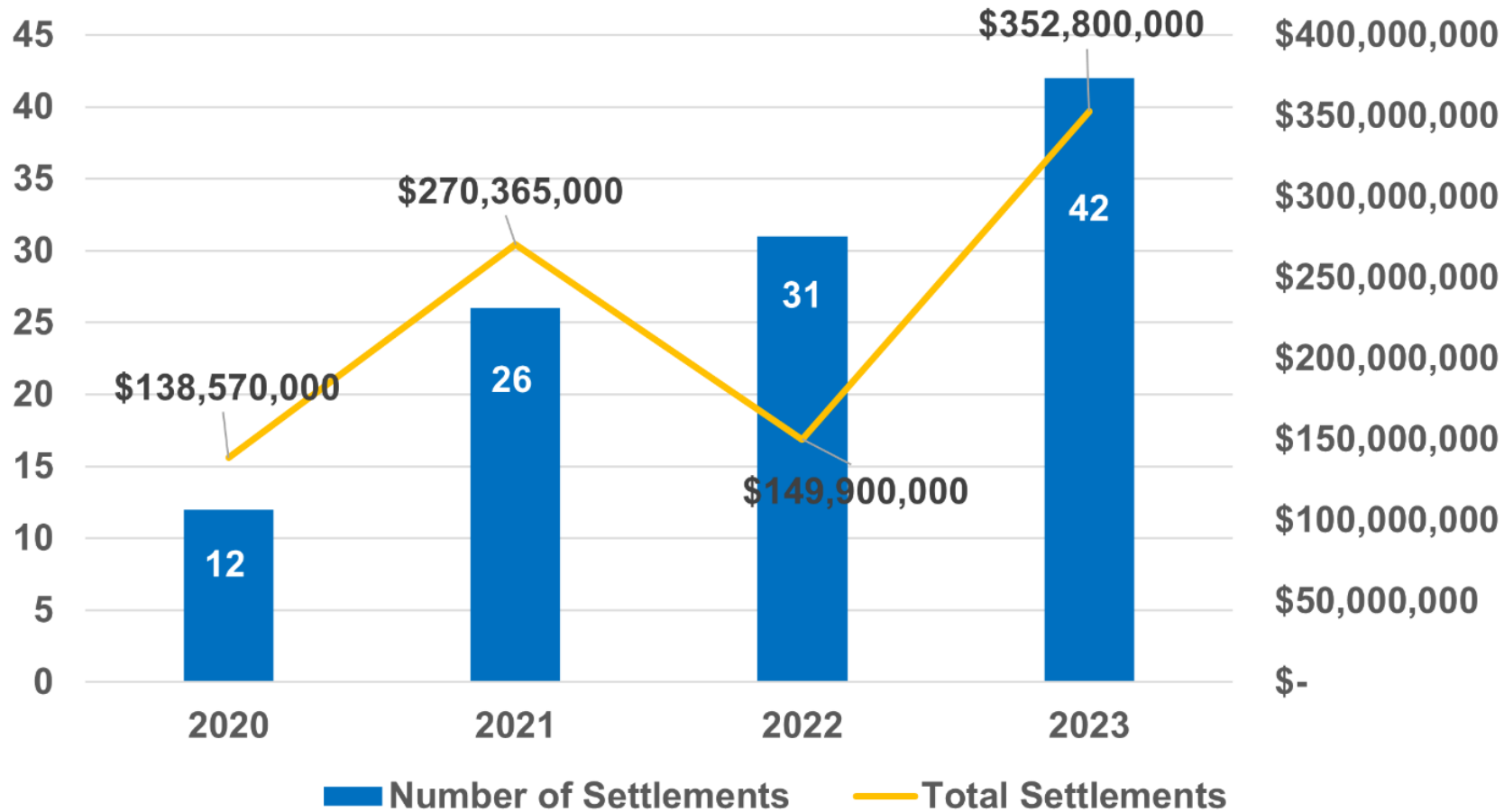


<u>Year</u>	<u>Number of Settlements</u>	<u>Total Settlements</u>	<u>Average Settlement</u>	<u>High</u>	<u>Low</u>
2020	12	\$ 138,570,000	\$ 11,500,000	\$ 20,900,000	\$ 2,400,000
2021	26	\$ 270,365,000	\$ 10,400,000	\$ 39,500,000	\$ 560,000
2022	31	\$ 149,900,000	\$ 4,800,000	\$ 32,500,000	\$ 330,000
2023	42	\$ 352,800,000	\$ 8,400,000	\$ 124,600,000	\$ 200,000
Total	111	\$ 911,635,000	\$ 8,200,000		

Average Settlements



Total Settlements



Ancillary Defense Issues

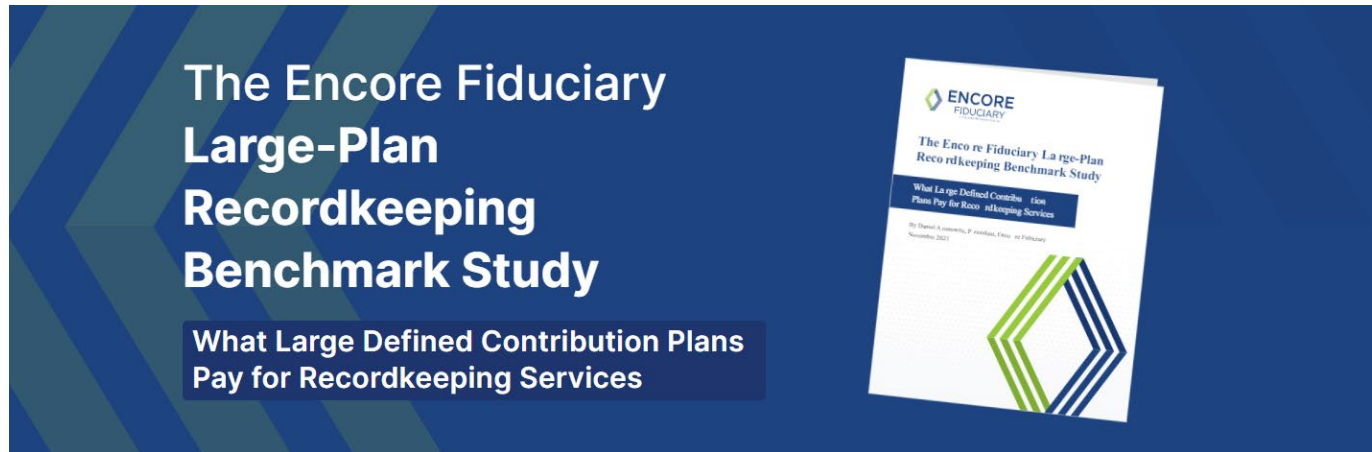


- Class Action Certification
- Arbitration of Participant Claims that involve plan-wide relief

Encore Fiduciary Risk Management



The Encore Large Plan Recordkeeping Database



- **The Encore Fiduciary Large-Plan Recordkeeping Benchmark Survey – What Large Defined Contribution Plans Pay for Recordkeeping Services** is designed to provide a reliable benchmark for plan fiduciaries to defend against imprudence lawsuits that are based on false and misleading comparisons.
- <https://encorefiduciary.com/recordkeeping-benchmark-study/>

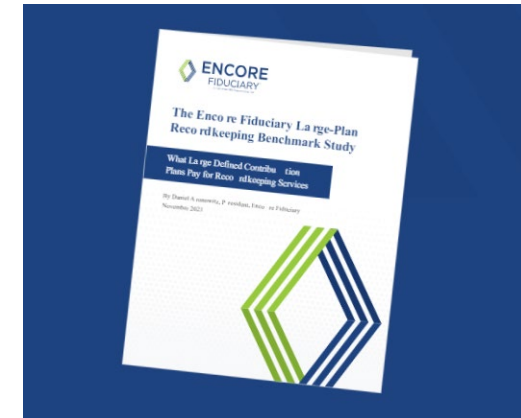
Save the Date – Upcoming Webinar on the Encore Recordkeeping Benchmark



- **Encore Fiduciary's Benchmark Survey on Recordkeeping Fees Webinar**
February 20th from 12:00-12:30 Eastern time.

- **Preview:** The Encore Fiduciary Large-Plan Recordkeeping Benchmark Survey – What Large Defined Contribution Plans Pay for Recordkeeping Services is designed to provide a reliable benchmark for plan fiduciaries to defend against imprudence lawsuits that are based on false and misleading comparisons.
- <https://encorefiduciary.com/recordkeeping-benchmark-study/>

- Invitation details to follow.



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[United Behavioral Health In the Supreme Court – When is Residential Treatment Covered as Medically Necessary?](#)

[The Paradox of The Yale Jury Finding Breach of Fiduciary Duty for Managing Recordkeeping Fees, But No Damages – The “Could Have” Versus “Would Have” Causation Standard](#)

[Debunking the Tyson Foods Excess Recordkeeping Fee Case](#)



Meet the Encore Team



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- Rebrand Euclid Fiduciary is now Encore Fiduciary & FAQ's:
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Euclid Fiduciary is Now Encore Fiduciary



A Few Notes about our Rebrand

Encore Fiduciary, formerly **Euclid Fiduciary**, is a division of **Specialty Program Group** that serves as a leading provider of fiduciary liability insurance for America's employee benefit plan sponsors and fiduciaries. The Encore Fiduciary team is known for its fiduciary expertise, thought leadership, and advocacy for America's plan sponsors.

- The Fid Guru Blog: <https://encorefiduciary.com/blog/>
- Rebrand & Website Page & FAQ's : <https://encorefiduciary.com/euclid-is-now-encore/>
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- **Important:** Please have your IT department whitelist our new @encorefiduciary.com email address we are implementing. Incoming to @encorefiduciary.com already works. We will implement outgoing soon.

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