Now & Next

Benefits Alert

April 22, 2024

Fifth Circuit reverses dismissal of ERISA Breach of Fiduciary Duty Claims

By Jen Squillario, Charles M. Dyke, Ian Taylor, and Adam Adcock

This ruling continues a trend of permitting ERISA breach of fiduciary duty share class claims to proceed past a motion to dismiss but diverges on the issue of recordkeeping fees.

What's the impact?

- The Fifth Circuit held that by not replacing a plan's retail shares with cheaper, allegedly identical institutional shares, the district court could reasonably infer that the plan's committee breached its duty of prudence under ERISA.
- Separately, the Fifth Circuit appears to have departed from other Circuits in concluding that plaintiffs adequately pleaded a claim for "high recordkeeping costs."
- ERISA fiduciaries should carefully document in publicly available documents the deliberative process used to reach and maintain investment-option and recordkeeping decisions.

The United States Court of Appeals for the Fifth Circuit in *Perkins v. United Surgical Partners International,*[i] recently revived a dismissed suit alleging that the defendant "implemented a flawed process" in choosing the plan's investment options and "failed to manage and mitigate the plan's recordkeeping costs." The Fifth Circuit's decision joins six other Circuit courts in permitting similarly pleaded share-class claims to proceed past a motion to dismiss. Potentially even more importantly, the decision may be a departure from other Circuit court decisions in finding the plaintiffs' recordkeeping allegations sufficient to withstand a motion to dismiss.

The Fifth Circuit permits share-class claims to proceed in line with other circuits

In *Perkins*, the plaintiffs, participants in United Surgical Partners International's 401(k) Plan, alleged that the plan's committee failed to select the lowest-cost shares for the plan, which demonstrated a "flawed process for selecting the [p]lan's investment options." The Fifth Circuit explained that "[b]roadly speaking," there were two classes of shares—(1) retail or investor and (2) institutional, and although the two classes were alleged to be identical, the retail share classes were more expensive.

Relying on decisions of the Ninth, Eighth, Seventh, Sixth, Third, and Second Circuits, the Fifth Circuit agreed with the plaintiffs that alleging that the plan had not invested in available, lower-cost share class for its investment options was sufficient to survive a motion to dismiss.

Of great significance to plan sponsors and fiduciaries, the Fifth Circuit found insufficient the defendants' argument that the obvious explanation for including the more expensive retail share classes "is that retail shares permit revenue sharing which, in turn, helps to defray and better allocate recordkeeping costs." The Fifth Circuit found that there was also a second plausible explanation—"that the [c]ommittee included retail shares in the [p]lan due to mismanagement." The court noted that the defendants' "argument that they 'obviously' included retail shares in the [p]lan to reduce recordkeeping costs is severely undercut by the [p]laintiffs' allegation that the [p]lan's recordkeeping costs were significantly *higher* than those of comparable plans."

Relying on *Matney v. Barrick Gold of N. Am.*, 80 F.4th 1136, 1149-52 (10th Cir. 2023), the Fifth Circuit agreed that such share-class allegations can be rebutted where documents referenced in the complaint contradict plaintiffs' allegations. But the documents referenced by the plaintiffs in this complaint appeared not to contradict the share-class allegations, the Fifth Circuit held. Had the committee's records or even potentially Form 5500 filings included evidence of the deliberative process the committee followed or documentation of its use of revenue sharing from the selected share classes to pay for recordkeeping costs, the motion to dismiss might have been granted.

Fifth Circuit seems to loosen the requirements for pleading recordkeeping claims

As for the plaintiffs' recordkeeping claim, relying on decisions from the Eighth, Seventh, and Third Circuits, the Fifth Circuit found it sufficient for plaintiffs simply to compare the plan's alleged recordkeeping costs with the recordkeeping costs of similarly sized plans (as measured by number of participants) and to allege that every plan's recordkeeping costs are "primarily dependent upon the number of participant accounts in the plan rather than the value of assets under management in the plan." Thus, if a plaintiff identifies a plan with a similar number of participants and lower alleged recordkeeping costs, she has a stronger chance of surviving a motion to dismiss despite failing to allege facts about the specific services rendered to the defendant's plan or its comparators.

Put another way, the Fifth Circuit did not require the plaintiffs to include "allegations about the specific services rendered in exchange for fees" for the plan at issue or the alleged comparator plans, which appears to be a departure from other courts requiring plaintiffs to plead a meaningful benchmark.[ii] As such, ERISA fiduciaries should maintain a current analysis of recordkeeping costs, and document regular efforts to minimize costs.

How can plan fiduciaries minimize litigation risk?

Plan fiduciaries should consult with counsel on proactive measures they can take to document—including in publicly available materials, such as Form 5500 filings—the extent to which revenue sharing provided by higher-cost share classes is used to defray recordkeeping expenses, which could greatly assist in defeating any inference of imprudence from the mere presence of such share classes in the plan.

Being prepared with evidence of prudent plan stewardship can help shut down a lawsuit without costly fact and expert discovery. Plan fiduciaries should regularly revisit and document such decisions to demonstrate continued prudence.

For more information on the content of this alert, please contact your Nixon Peabody attorney or:

Jen Squillario
202.585.8078
jsquillario@nixonpeabody.com

Charles M. Dyke
415.984.8315
cdyke@nixonpeabody.com

Ian Taylor
202.585.8077
itaylor@nixonpeabody.com

Adam Adcock
202.585.8092
aadcock@nixonpeabody.com

[i] *Perkins v. United Surgical Partners International,* No. 23-10375, 2024 WL 1574342 (5th Cir. Apr. 11, 2024).

[ii] *See, e.g., Smith v. CommonSpirit Health*, 37 F.4th 1160, 1169 (6th Cir. 2022); *Matousek v. MidAmerican Energy Company*, 51 F.4th 274, 279 (8th Cir. 2022).