

Seventh Circuit Affirms Dismissal of Challenge to 401(k) Fee Arrangements

In the first federal appellate court decision addressing challenges to fee arrangements with and among 401 (k) service providers, the Seventh Circuit has affirmed a Wisconsin district court's dismissal of a complaint against Deere & Co., Fidelity Management Trust Company and Fidelity Management and Research Company. Perhaps of equal significance was the circuit court's confirmation of an award of attorneys' fees against the plaintiffs in the amounts of \$54,396.57 for Deere and \$164,814.43 for the Fidelity defendants. Awards of attorneys' fees against plaintiffs are rare in ERISA cases, and the amounts awarded in this case are certainly noteworthy.

In autumn 2006 a plaintiffs' law firm in St. Louis filed a series of substantially identical complaints against a number of large, prominent employers, challenging the mutual fund fees charged to participants in 401(k) plans sponsored by those employers. A number of the actions, such as this one against Deere and Fidelity, were expanded to include service providers as defendants. Similar complaints have since been filed by other plaintiffs' attorneys. In substance, these complaints typically claim that the plan sponsors and other plan fiduciaries violated their fiduciary duties under ERISA by (i) providing investment options that charge excessive and unreasonable fees and costs, and (ii) failing to disclose sufficient information to plan participants about the fees and costs, notably information relating to revenue sharing arrangements among plan service providers. The Seventh Circuit's decisions in ERISA matters are generally well respected, so this result in favor of Deere and Fidelity may be expected to influence a number of these other pending cases.

The Deere 401(k) plan offered 26 core investment options, of which 23 were Fidelity mutual funds, two were investment funds managed by Fidelity Management Trust Company, and one was a Deere company stock fund. The plan also provided a mutual fund brokerage window through which participants could choose among 2,500 other Fidelity and non-Fidelity funds. Fidelity Management and Research Company advised the Fidelity mutual funds offered by the plan. Although Fidelity Management Trust Company counseled Deere about which investment options to include in the plan, the final selection was made by Deere. Deere and Fidelity agreed, however, that the core investment options would be limited to Fidelity funds.

The plaintiffs argued that the roles played by the Fidelity defendants in the selection of investment options made them "functional fiduciaries" of the plan. The court rejected this argument, noting that Deere's final authority over fund selection made it the sole fiduciary in that regard. "Playing a role" in that process did not elevate the Fidelity defendants to fiduciary status. The plaintiffs also focused on the revenue sharing arrangement between the Fidelity defendants and argued that the determination by Fidelity Management and Research Company of the amount of revenue it shared with Fidelity Management Trust Company gave the former control over the disposition of plan assets. The court observed, however, that the revenue shared between the Fidelity defendants was drawn from the assets of the mutual funds advised by Fidelity Management and Research Company. The revenue in question, accordingly, was Fidelity's assets, not plan assets. On these grounds the court dismissed the complaint against the Fidelity defendants in its entirety.

Turning to the claims against Deere, the Seventh Circuit likewise dismissed the complaint in its entirety for the following reasons:

- Deere had no fiduciary duty to inform participants of the revenue sharing arrangements between the Fidelity defendants. No such disclosure was required by ERISA or governmental regulations. In fact, regulations that were proposed by the Department of Labor in July 2008, for disclosure of plan fees and expenses to participants, confirm that disclosure of revenue sharing arrangements generally will not be required. The court observed that participants received disclosures of the total fees and expenses charged by each of the core investment funds. The subsequent allocation of those fees and expenses among various entities was

not material to participant investment decisions.

- The availability of more than 20 Fidelity mutual funds as core investment options and 2,500 other funds through a brokerage window effectively rebutted any claim that Deere violated its fiduciary duty by selecting investment options with excessive fees. The fees charged by the available funds ranged from .07% to a bit more than 1%. These fees were disclosed to participants, and the available investment options provided participants with a sufficient range of alternatives to allow them to effectively control their risk of loss. Deere otherwise satisfied the criteria of section 404(c) of ERISA and its regulations, so Deere was relieved of any fiduciary responsibility relating to participant choices among the available investment options.
- Nothing in ERISA or its regulations prohibits limiting plan investment options to a single family of mutual funds.
- Without deciding the issue, the court questioned whether the selection of plan investment options was a fiduciary responsibility at all, suggesting that it may instead be a plan design decision outside the fiduciary realm. This suggestion is directly contrary to arguments by the Department of Labor in its amicus brief to the Seventh Circuit. The Department has long maintained that the selection of plan investment options is a fiduciary function. It stated this position in 1992 in a footnote to the preamble to the final regulations under ERISA section 404(c). In an effort to strengthen and formalize its position, the Department proposed in July 2008 to amend the regulations under section 404(c) to incorporate into the regulation itself the principle that a fiduciary has a duty "to prudently select and monitor any designated investment manager or designated investment alternative offered under the plan." The Seventh Circuit's suggestion, however, indicates that courts may not always feel bound by the legal interpretations of regulatory agencies.

If you have questions or would like additional information about fiduciary issues relating to mutual fund fees and other plan administrative expenses, please feel free to contact Brian Dougherty at (215) 587-5919 or bdougherty@postschell.com.

Disclaimer: this E-Flash does not offer specific legal advice, nor does it create an attorney-client relationship. You should not reach any legal conclusions based on the information contained in this E-Flash without first seeking the advice of counsel.

© Copyright 2009 Post & Schell, P.C. All rights reserved
"POST & SCHELL" and the Post & Schell Logo are registered trademarks of Post & Schell, P.C.
[About Us](#) | [Our Attorneys](#) | [Practice Areas](#) | [Publications](#) | [Offices](#)