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CAB 15-6

CLIENT ACTION Bulletin
Employee Benefits

Supreme Court Ruling Calls Attention to the Fiduciary Duty to Monitor 401(k) Plan Investments

SUMMARY

The U.S. Supreme Court unanimously held that although the initial selection of plan investments occurred beyond ERISA's six-year statute of limitations, a lawsuit by participants in a 401(k) savings plan may proceed on whether the plan fiduciaries breached their continuing duty to monitor and remove imprudent trust investments (*Tibble v. Edison Int'l* (No. 13-550, 5/18/2015)). In so ruling, the Court found that a lawsuit against plan fiduciaries is timely filed if the participants' claim alleging a breach of the continuing duty to monitor occurred within six years. The Court's ruling may spur lawsuits by participants over plan fees.

DISCUSSION

The Facts of the Case

Edison International sponsors a 401(k) savings plan for its employees that includes a number of investment options. The plan participants claimed in 2007 that the company's fiduciaries violated ERISA's duty of prudence by offering, beginning in 1999, "retail" class shares of three mutual funds instead of less costly "institutional" class shares of the same funds. The federal district court in which the lawsuit was originally filed ruled that the plaintiffs' claims against the employer were time barred by ERISA's six-year statute of limitations and that circumstances had not changed sufficiently within that period to place the fiduciaries under an obligation to review the funds.

On appeal to the U.S. Court of Appeals for the Ninth Circuit, the plan participants asserted that their claims were timely, because the plan retained those same class shares offered in 1999. The Department of Labor supported the claim of the participants, saying that a "continuing violation" theory provided an exception to the claims filing period and arguing that ERISA fiduciaries would have no incentive to remove imprudent investments otherwise. The Ninth Circuit concluded, however, that the plaintiffs did not present facts showing that a change in circumstance triggered a fiduciary obligation to conduct a full review of the 1999 funds within the six-year statutory period under ERISA.

The Supreme Court's Decision

The Supreme Court determined that the Ninth Circuit (and other lower courts) failed to "recognize that under trust law a fiduciary is required to conduct a regular review of its investment with the nature and timing of the review contingent on the circumstances." Trust law – from which ERISA's fiduciary duty is derived – provides a continuing obligation on fiduciaries "to monitor trust investments and remove imprudent ones," the Court noted. Thus, the lower courts applied the six-year limitation period solely on the employer's initial selection of the funds without considering the duty to monitor the investments. In this particular case, if the suit alleging a failure to monitor the investments occurred within the six years of the suit's commencement, the Court opined that the claim was timely.

The Court sent the case back to the Ninth Circuit to consider whether the fiduciaries breached their duties to monitor the funds within the six-year period, recognizing the importance of trust law in applying ERISA's fiduciary standards.

ACTION

Although the Court's ruling does not provide guidance on what constitutes appropriate monitoring of investments, it clearly demonstrates the need for plan fiduciaries to review investment options on some regular basis; they may not select an option and at no time revisit that investment selection. Reviews should consider whether an investment option remains prudent, taking into account costs, fees, suitability, and benchmarks, among other factors. Plan sponsors also should review plan documents and investment policies and consider taking steps to address the frequency of reviews and the removal of imprudent investments. A plan sponsor's investment committee should document its investment option selections (e.g., the reasons for selecting retail over institutional class shares) and its monitoring activities, as well as maintain records of its compliance efforts.

For additional information about the U.S. Supreme Court's ruling, please contact your Milliman consultant.